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**PRIMER BOOK OF  
COMMERCIAL LAW**

BY

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*Dedicated to My Father*  
**AKSHOY KUMAR SEN, B. C. S.**  
*and My Brother*  
**SUKUMAR SEN, I. A. S. .**

*To whose noble example and inspiring  
guidance I owe my everything.*



## FOREWORD

. I am glad to see this book written by one of my own juniors, Mr. A. K. Sen. I have gone through this book and I have been highly impressed by the way in which Mr. Sen has brought, within the scope of a single book, all the varied branches of Commercial Law. I am sure this book will prove indispensable not only to commerce students but also to all beginners in the study of law

Bar Library,  
Calcutta  
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S. R. Das  
Barrister-at-Law.

## FOREWORD

I have carefully read through *Hand Book of Commercial Law* by Mr. A. K. Sen, and I have been very much struck by some of the special features. Apart from the fact that the book presents the whole subject in a handy form, the manner in which difficult topics have been treated is admirable. The canvas is small, but the picture that the author presents of his subject is distinct. The volume is sure to do immense good to students, both serious and casual. To be able to breathe life into the dry bones of Commercial Law is no small feat, and Mr. Sen has achieved it perfectly.

Arun Kumar Sen, M.A., M.Sc.  
(Econ.), London, Barrister-at-Law,  
Vice-Principal, City College,  
Commerce Department,



## PREFACE TO THE THIRD EDITION

The second edition of this book was very well received and the stock was completely exhausted within a year. I, therefore, feel encouraged to bring out the third edition of this book. The chapters on Insurance and Law of Carriage have been altered beyond recognition and I feel confident that they will be appreciated by students and practitioners alike. A new chapter on Bankers and Banking has been added and I am sure it will serve the needs of students and bankers on this subject. The latest decisions both in India and England have been incorporated in this edition. The case of Naresh Chandra Sanyal *vs.* Calcutta Stock Exchange Association referred to in the chapter on Company Law has been reported in 49 C.W.N. at p. 502, under the title "Naresh Chandra Sanyal *vs.* Ramani Kanto Ray". As the manuscript of the third edition of this book was already in the press the reference of the case could not be given in the book.

I cannot conclude this introduction without expressing my thanks to many sincere friends, teachers and members of the Bar who have given me valuable help and suggestions.

Bar Library Club,  
High Court, Calcutta,  
16th July, 1945.

Author

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## INTRODUCTION

### Nature of Commercial Law :

(The Commercial Law of India has been mostly borrowed from English Law.) Merchants have long forgotten the pre-British Hindu and Mahomedan law relating to contracts, sale etc. To understand the nature of Indian Commercial Law prevailing today, we have to probe into the genesis of English Commercial Law. (The English Commercial Law is a product of history and has grown out of what has long been known as the *Law Merchant* or *Lex Mercatoria*.) Nobody has yet been able to trace the actual course through which the *Lex Mercatoria* developed as a distinct body of law recognised by courts of law. But it is sufficient to note here that in its essence and structure it is a body of customs and usages which have been developed in course of the mercantile history of Western Europe, enriched at every stage by copious borrowings from Roman Law and from principles of equity and good conscience. (In its growth it has received contributions from every country of Western Europe and it has always been regarded as a *jus gentium* or the law of nations.) "When Butler J. spoke in *Master v. Miller* (1791), 4 Term Rep. 340, of the *lex mercatoria* as a system of equity, founded on the rules of equity, and governed, in all its parts, by plain justice and good faith"; when it was said that it was impossible that 'the maritime laws of any one realm should be sufficient for the ordering of affairs and traffic of merchants'; that the *law merchant* is a law 'whereof all nations do take special knowledge' there was not merely a reference to the absence of technicalities, but to the fact that the same rules of law were generally applied throughout civilised Europe.<sup>1</sup> Speaking of Negotiable Instruments K. Bhasyam<sup>2</sup> says, "The origin of these instruments can be traced to the usage and custom of merchants and traders which courts of law have accepted as settled law, in view of the general interests of trade and the convenience of the public." It may be equally said of Commercial Law that it can be traced to the usage and custom of traders and merchants, which has been recognised by statutes and courts of law and has

<sup>1</sup> Smith's Mercantile Law, 18th ed., p. ccvii.

<sup>2</sup> Bhasyam & Adiga's—The Negotiable Instruments Act, 18th ed., p. V.

been adapted as settled law, in view of the general interests of trade and the convenience of the public.

The term Commercial Law does not lend itself to an easy definition. Taking from the definition in the Rules of the Supreme Court in England, Ch XII Rule I of the Rules of the Calcutta High Court (original side)<sup>1</sup> defines commercial suits as follows—"Commercial suits include suits arising out of the ordinary transactions of merchants, bankers and traders, amongst others, those relating to the construction & mercantile documents, export or import of merchandise, affreightment carriage of goods by land, insurance, banking and mercantile agency, and mercantile usages, and debts arising out of such transactions." From this we can shape our definition of Commercial Law as follows—Commercial Law includes the law applicable to the ordinary transactions of merchants, bankers and traders, and denotes that branch of the law which relates to the rights of property and the relations of persons engaged in commerce.

It is also difficult to enumerate what are to be regarded as the different branches of Commercial Law. The same law may relate to commercial as well as extra commercial transactions. The law of contract for instance applies to merchants and non merchants equally. For the sake of convenience the following branches are usually included in Commercial Law—(a) Law of contract, (b) Law relating to sale of goods, (c) Partnership law, (d) Company law, (e) Law of Insurance, (f) Contract of affreightment, (g) Law relating to carriage of goods by land, (h) Law relating to commercial securities, (i) Law relating to arbitration, (j) Law of Banking and (k) Law relating to negotiable instruments.

### **History of Commercial Law :**

It has already been noticed that Commercial Law grew out of the *Law Merchant*. In England before the end of the thirteenth century the *Law Merchant* was already conceived as a body of rules which stood apart from the Common Law. But it seems to have been rather a special law for mercantile transactions than a special law for merchants. It would, we think, have been found chiefly to consist of what would now be called rules

<sup>1</sup> Ormond's, "The Rules of the Calcutta High Court," p. 396.

of evidence, rules about the proof to be given of sales and other contracts, rules as to the legal value of the tally and the God's penny.<sup>1</sup> These special rules were supposed to have been known to all the merchants. The merchants used to assemble in the fairs and markets of mediæval times and declare the law. The law used to be administered in fairs and markets by mercantile courts composed of merchants. Procedure was informal and justice was summary. The law administered by these courts was purely commercial and influenced by their composition. From the records of these courts we find that "cases turning upon the contract of sale are the most numerous. The contract was generally made by the agreement of the parties evidenced by the gift of a God's penny or earnest money."<sup>2</sup> We also find cases relating to fore-selling, selling out of the fair, selling without a proper display, or using false measures. Cases of contracts are also numerous. We also come across cases of theft, trespass and assault. The rules obtaining in the fairs were by no means purely English. They were supposed to have been known to merchants throughout Christendom and may as such be considered as *jus gentium* or the law of nations.

The market and fair courts disappeared towards the seventeenth century but the customs and usages developed by them were taken over by the Common Law Courts and gradually absorbed and enlarged. This marks the beginning of the real birth of Commercial Law in England. "By far the larger part of our modern commercial and maritime law is due to the reception of continental doctrines in the sixteenth and seventeenth centuries. In the case of commercial law this reception was effected partly by legislature, partly by the council, and partly by the various courts of law which had jurisdiction in mercantile cases—the Admiralty, the Chancery, the Star Chamber, and the Courts of Common Law. Through these various agencies many new legal doctrines, familiar in the trading centres of Europe, became part of English law, and began to be developed on native lines by the English Courts."<sup>3</sup>

Commercial Law has not, by any means, reached its last stage. The exigencies of trade are continually expanding and the courts

<sup>1</sup> Pollock & Maitland—History of English Law, p. 467.

<sup>2</sup> Holdsworth's History of English Law, vol. 5, p. 109.

<sup>3</sup> Holdsworth's History of English Law Vol. 5, p. 102.

of the country are not to be slow in according recognition to the expeditious devised by traders for satisfying them. The legislature is also alert to initiate statutes to meet the growing needs of commerce and trade.

### cial Law :

The sources of Commercial Law may be grouped under the following heads :—

(a) The collection of maritime usages and customs—These were known as *coutumiers* and were compiled for the use of merchants and lawyers. They commanded great authority in the fourteenth and the fifteenth<sup>th</sup> centuries in Europe. They may be divided into two categories—(i) those which were collected in the Mediterranean ports, and (ii) those which were compiled for the merchants in Northern Europe.

(b) Roman Law—In all difficult cases where custom and usage failed to afford any solution reference was made to Roman Law to cover the deficiencies of the law of every civilised country. “The writers on mercantile law, here (England) and in the continent, sought in Roman Law solutions for difficult and novel problems and often found them”<sup>1</sup>

(c) Equity—Where custom failed and Roman Law afforded no help English judges applied the principles of equity and good conscience. The law relating to disclosure in contracts of insurance and other contracts *uberrimae fidei* is an example or the point.

(d) The Fair Court—The principles evolved in the fair courts of the mediæval times were gradually absorbed in the body of Commercial Law.

### of Indian Commercial Law :

The sources of Indian Commercial Law are the following—

(a) Statutes—Statutes laying down law on the basis of English law form by far the most important source of Indian Commercial Law. The Contract Act, The Sale of Goods Act, the Partnership Act, and the Companies Acts are instances of the way in which English Commercial Law has gradually been introduced in India.

<sup>1</sup> Smith's Mercantile Law, 13th ed., p. ccxv.

(b) English Common Law—Where Statutes are absent and where Statutes are ambiguous the Indian Courts of Law are always ready to apply the English law on the subject. Even in interpreting statutes, reference is always made to English decisions.

(c) Indian Custom and Usage—Where there is a universal custom of ancient origin, such custom, unless otherwise excluded, always governs commercial transactions. The law relating to hundies and the law of dampdut� prevailing in Bengal are illustrations on the point.

(d) Equity—Equity in India as in England always gives a residual power to Courts to deal with harsh cases where the ordinary laws fail to give any solution.



# **Hand Book of Commercial Law**

**PART I**



# **COMMERCIAL LAW**

## **CHAPTER I**

### **LAW OF CONTRACT**

#### **Contract**

The law of contract may be described as the endeavour of public authority, a more or less imperfect one by the nature of the case, to establish a positive sanction of Contract.

for the expectation of good faith, which has grown up in the mutual dealings of men of average right-mindedness. Accordingly the Indian Contract Act defines a contract as an agreement enforceable by law. The most characteristic feature of a contract is that it usually creates a right not to thing but to another man's conduct in the future—though some classes of contract like pledge or hypothecation create rights in things. "He who has given the promise is bound to him who accepts it, not merely because he had or expressed a certain intention, but because he so expressed himself as to entitle the other party to rely on his acting in a certain way."<sup>2</sup> The obligation whereby a person will be bound by his promise to another can only be created by an agreement which the law will enforce. We have, therefore to see what is an agreement and what agreements will be enforced by law.

#### **What is a Contract :**

Section 2(a) of the Indian Contract Act defines a contract as an agreement enforceable by law. This definition naturally divides itself into two distinct parts. First of all, there must be an agreement; secondly, such an agreement must be enforceable by law. Let us, however, proceed to define and analyze all these three elements which go to make up an agreement and then the question will arise how far such an agreement must be satisfied in order to make such an agreement enforceable by law.

### Agreement :

An agreement and a promise are one and the same thing.

According to S 2(e) of the Indian Contract Act  
Agreement and every promise and every set of promises forming  
the consideration for each other, is an agreement

An agreement or promise is an act in the law whereby two or more persons declare their consent as to any act or thing to be done or foreborne by some or one of those persons for the use of the others or other of them. Such declaration may take place by (a) the concurrence of the parties in a spoken or written form of words as expressing their common intention, or (b) an offer made by some or one of them and accepted by the others or other of them. In every case an agreement or promise ultimately resolves itself into an offer or proposal made by one party and accepted by the other. When one person signifies to another his willingness to do or to abstain from doing anything, with a view to obtaining the assent of that other to such act or abstinenace, he is said to make a proposal or offer. When the person to whom the proposal is made signifies his assent thereto, the proposal is said to be accepted. When the proposal is accepted the two minds are *ad idem*. A proposal when accepted becomes a promise or an agreement. The person making the proposal is called the "promisor" and the person accepting the proposal is called the "promisee". A says to B, "Will you sell me your land Blackacre for £100?" A is making an offer or proposal. B says, "yes" B accepts the offer. The two minds are *ad idem*. There is a promise or agreement which binds both A and B.

An agreement may be either *express* or *implied*. An *express* agreement is made whenever there is an offer coming from one party which is accepted by the other. Let us take an illustration. A says to B, "Will you sell me your land Blackacre for £100?" B says "yes". In this case A has made an offer or proposal which B has accepted. The two minds are in agreement or *ad idem*, as it is called, at some one time with regard to what is to be done by both or one. An agreement will thus be constituted whenever a person makes an offer and another accepts it as a result of which the two minds are brought in harmony or agreement.

## LAW OF CONTRACT

An implied agreement differs from an express agreement in that in its case the act of offer and the act of acceptance are not clearly expressed either verbally or in writing but implied Agreement have to be gathered from the conduct of the parties or from surrounding circumstances, such as the general course of dealing between the parties or any general or local customs which may fairly be assumed to have guided the conduct of the parties. If A mentions a figure at an auction bid he is deemed in law to have made an offer. If the auctioneer drops his hammer his conduct implies that he accepts A's offer. So also, if the Judd Company run a Bus in Calcutta from the Likes to Shambazar which stops to take up and set down passengers it implies that the Company is making an offer to carry any member of the public to any place on the route at the stated fare. If any person gets on the bus he is presumed by law to have accepted the offer to pay the fare which is due for the distance he wants to travel.<sup>1</sup>

### Offer :

A person is said to make an offer when he signifies to another his willingness to do or to abstain from doing anything, with a view to obtaining the assent of that other to such an act or abstinence. An offer becomes complete when it is communicated to the offeree. Without such communication, the offer is of no effect so far as the offeree is concerned.

Sometimes a person declares his intention to make an offer but does not actually make an offer. In this case such a declaration may not be accepted and thus turned into an agreement. Thus, Offer distinct in the case of *Harris v. Nickerson*<sup>2</sup> the defendant furnished from advertised that he would sell by auction certain furniture at a place some distance from London make an offer. The plaintiff went from London to the appointed place and found the sale withdrawn. He, thereupon, sued the defendant for breach of contract. It was held that the defendant's advertisement simply declared his intention to make an offer to any intending buyer. It could not therefore, be accepted by acting upon it as in the case of *Carhill v. Carbolic Smoke Ball Co.*<sup>3</sup>

<sup>1</sup> *Poyer v. Care*, (1787) 3 T.R. 148. *Frost v. Sheldens Dairies Co.*, (1805) 1 R.D. 603.

<sup>2</sup> (1873) L.R. 8 Q.B. 286.

<sup>3</sup> (1893) 1 Q.B. 254.

An offer should also be distinguished from an invitation to make an offer. When a shopkeeper issues a price list or places <sup>Invitation to make an offer</sup> priced goods in his shop window, he is not deemed in law to make an offer to sell at the named prices or to sell it all. In both cases it is an invitation to intending purchasers to make an offer. Persons asking for tenders do not in the same way make any offer which can be accepted. They simply invite suppliers to make offers which they can accept.<sup>1</sup>

(An offer must be made known to the offeree to enable him to accept it and form a binding agreement.) There cannot be any agreement or acceptance unless the offer has been communicated to the offeree. Thus, if A declared a reward for <sup>Communication of an offer</sup> the recovery of his lost dog, he is not bound to pay any one who finds his dog in ignorance of the reward. The finder in this case cannot be deemed to have accepted A's offer by acting upon it since he had no knowledge of the offer. The finder of the lost dog can only get the reward if he knew of A's offer previously to his so finding.<sup>2</sup>

It is now a settled principle of law in India that if a man performs the conditions of a proposal made by another in ignorance of the proposal itself, the person who thus performs the conditions of the proposal cannot be deemed to have accepted the proposal and thus to be entitled to any benefit under the contract. In *Lalmon Shukla vs Gowri Dutt*<sup>3</sup> the High Court of Allahabad formally laid down this principle. The Plaintiff in that case was in the Defendant's service as a Muni. On the Defendant's nephew having absconded the Plaintiff volunteered to search for the missing boy. In his absence the Defendant offered a reward of Rs 50/- to any one who might bring back the boy. Subsequently the Plaintiff found the boy and claimed the reward. It was proved that the Plaintiff did not know of the offer for reward when he made the search and found out the boy. It was held that the Plaintiff was not entitled to the reward. In this instance the Allahabad High Court, following the recent English decisions, declined to follow the English case of *Wilham vs Carwardine*.<sup>4</sup>

<sup>1</sup> *Harvey v Facey* (1893) AC 552

<sup>2</sup> Section 4

<sup>3</sup> (1930) 11 All LJ 489

<sup>4</sup> (1834) 4 B & A 631

for a car given by B to A. Giving of the car is said to be the consideration for A's promise,—it is a benefit which A gets in return for his promise. It would be the same if A promises to pay £100 if B will promise to give his motor car in return. In this case, as noted before, the consideration for a promise is a promise and B, by accepting the offer, can compel A to perform the contract and if A fails, to sue him for breach of contract.

There are certain rules regarding consideration in English law —(1) Consideration need not be adequate. This means that the court will not enquire whether the consideration in a particular case, that is, what has been done, forthcoming or promised, is equivalent in value to the promise of the promisor. The minutest consideration is enough provided it has some value in the eye of law. Thus if A promises to pay £100 to B for an old stamp which B gives to A, it will be no defence of A in answer to B's claim that the stamp in actual fact was of a much smaller value.

(2) Consideration must be real and not sham. This means that the consideration must be of real value and not one which is only of apparent value. Thus if A promises to pay B £100 in consideration of B's promise to take him to the moon, the consideration is sham and not real as B's promise is absurd. Similarly, suppose A owes B £100 and A offers to pay £90 down in full settlement. B accepts and A pays £90 in full settlement. Nevertheless, B can sue for the unpaid balance of £10 as his promise to accept £90 in full settlement of a debt of £100 is really a promise to forego his claim to the odd £10, and there is no consideration for that. But now, suppose that A's debt is payable in future, say 3 months hence, and A offers £1 down. If B takes this, there is consideration for his giving up odd £99 for his getting £1 three months sooner than he is entitled to it.

(3) Consideration must not be illegal. This means that any promise or act or forbearance which is against law or public policy cannot be the consideration for another promise.

(4) Consideration must not be past. A past consideration, that is one which is wholly executed before the promise is insufficient to support a subsequent promise. Thus, if I offer Rs. 10/- to B, if he will run from Dum Dum to Calcutta, then B, by actually running from Dum Dum to Calcutta, will simultaneously accept the offer and execute the consideration, and I shall

be bound to pay him Rs. 10/- But if I promise B Rs. 10/- in consideration of his having run from Dum Dum to Calcutta last week, the consideration is past. It is something done before the offer and such consideration will not be able to support a binding contract in English law.

5. Consideration must move from the promisee, i.e., consideration must move from the party entitled to sue on the contract. This rule is expressed by the maxim "No stranger to the consideration can sue on the contract." Suppose A promises to pay money to C in consideration of B's promising to build a house. B builds the house. C cannot sue A on the promise because he has neither done nor foreborne, nor suffered anything nor made any promise in return for A's promise.

According to the Indian Contract Act a consideration has been defined as follows<sup>1</sup>:

"When at the desire of the promisor, the promisee or any other person has done or abstained from doing or does or abstains from doing, or promises to do or to abstain from doing something, such act or abstinence or promise is called a consideration for the promise." On the face of it, this definition makes a departure from the English law on two fundamental points, viz., (1) the words "promisee or any other person" implies that consideration may move either from the promisee or from some one other than the promisee. Thus in Chinni v. Rammayi<sup>2</sup>, the facts were as follows:

A, by a deed of gift, made over a certain property to her daughter on condition that the daughter should pay an annuity to A's brother. It had been done by A. On the same date the daughter executed in writing in favour of the brother, agreeing to pay the annuity. The daughter having declined to fulfil her promise, the brother sued the daughter to recover the amount due under the agreement. It was contended by the daughter that no consideration proceeded from the brother and that he, being a stranger to the consideration, had no right to sue. It was held that the consideration indirectly moved from the brother to the daughter and that he was, therefore, entitled to maintain the suit. But though consideration may move from a third party,

<sup>1</sup> Section 2 (d).

<sup>2</sup> (1891) 4 Mad. 137.

it should be remembered that a person who is not a party to the agreement cannot sue on the agreement.

(2) The words 'has done' or abstained from doing, declare the law to be that an act done by A at B's request without any contemporaneous promise from B at the time, may be a consideration for a subsequent promise from B to A. This clearly shows that in India past consideration is a good consideration. Thus in *Sindhu v. Abraham*<sup>1</sup>, the Plaintiff rendered service to the Defendant at his desire expressed during his minority and continued doing him service at the same request after his majority. The question arose whether such service constituted a good consideration for a subsequent expressed promise by the Defendant to pay in annuity to the Plaintiff. It was held that the agreement which was for compensating for past services rendered, was a valid one under Section 2 of the Indian Contract Act.

The Indian law regarding consideration also differs from the English Law in that certain agreements without consideration are, nevertheless, valid. These agreements are (1) a gratuitous promise is binding if it be in writing and registered and if it be made on account of natural love and affection between parties standing in a near relation to each other. (2) A gratuitous promise is also binding when it is a promise to pay a time-barred debt, though without any consideration, provided the promise is in writing and signed by the promisor or his duly authorised agent. (3) A promise to compensate, wholly or in part, a person who has already voluntarily done something for the promisor, is enforceable, even though it is without consideration. (4) A promise to compensate fully or in part a person who has already done something voluntarily which the promisor is legally compelled to do, is a valid contract.

#### **Exception to the rule "no Consideration no Contract."**

Section 25 of the Indian Contract Act makes a significant departure from the English law in that it dispenses with consideration in the following cases of contracts which are valid and binding, even though they are made without consideration:

1. Where the contract is expressed in writing and registered under the law for the time being in force for the registration

of documents and is made on account of natural love and affection between parties standing in a near relation to each other. This naturally forms an exception to the rule that a mere gratuitous promise is void. It states that a gratuitous promise made for natural love and affection by parties standing in a near relation to each other is valid, unless, of course, it is induced by fraud or misrepresentation. In every case, however, natural love and affection has to be proved and parties standing in a near relation to each other, do not necessarily imply 'mere relatives.' Thus in *Mrs. X. vs. Mr. X.*<sup>1</sup> a promise by the husband to provide maintenance to the wife was declared void, as it was obvious in that case that no natural love and affection existed between the husband and the wife. It should be remembered that a gratuitous promise under this provision can only be enforced provided it is in writing and is registered.

2. Where the contract is a promise to compensate, wholly or in part, a person who has already voluntarily done something for the promisor A finds B's purse and gives it to him. B promises to give A £50. A can enforce the promise. It should be remembered in this connection that past services rendered *at the desire of the promisor* is a good consideration under Section 2 of the Indian Contract Act. But this Section (S 25) deals with past services rendered voluntarily and provides that, though such services do not form a good consideration, yet a promise based on it is nevertheless enforceable. Thus in *Kalipadhi vs Durgadas*<sup>2</sup> it was held that where certain services were rendered by a pleader, on request and in pursuance of an agreement to pay a certain remuneration, the services rendered not being voluntary, the agreement could not be treated as a promise to compensate under this section, but an agreement based on good consideration under Section 2?

3. Where the contract is a promise to compensate, wholly or in part, a person who has already voluntarily done something which the promisor was legally compellable to do. A supports B's infant son. B promises to pay A's expenses in so doing. As the promise is based on A's voluntarily doing something which B was legally compellable to do, A can enforce the promise.

<sup>1</sup> 98 I.C. 217.

<sup>2</sup> 37 C.W.N.

4. Where the contract is a promise to pay a time barred debt without consideration, provided the promise is in writing and signed by the promisor or his duly authorised agent. According to the statute of limitation a debt cannot be recovered by the creditor after the period of limitation has expired, unless the debtor or his authorised agent acknowledges the debt or makes payment either towards principal or interest before the expiration of the period of limitation<sup>1</sup>. But this section gives the creditor the right to enforce payment of the debt, even after the expiration of the period of limitation and even in the absence of acknowledgement or payment provided the debtor or his duly authorised agent promises in writing after the expiration of the period of limitation to repay the debt. The subsequent promise in this case though without consideration is valid and enforceable.

5. Where the contract is a promise to appoint an agent. According to the Section 185 of the Indian Contract Act the contract of agency require no consideration.

#### **Other Elements of a Valid Contract :**

According to Section 10 of the Indian Contract Act a contract is valid when (1) the parties to it are competent to contract, (2) the agreement is brought about by free consent and (3) the consideration and object are lawful.

#### **1. Parties Competent to Contract :**

1. Every person is not competent to enter into a valid contract. Thus contracts entered into by (1) minors and (2) persons of unsound mind are void.

#### **Contracts by Minors :**

According to the English law an infant is a person who is below the age of 18 years. In the common law of England an infant contract was either valid or voidable. It was valid when it was for necessities and in for the benefit of the infant. It was voidable at the option of the infant when the contract was neither for necessities nor for the benefit of the minor. Thus an infant was, by common law, liable to pay for necessities sold or delivered to him and thus was also entitled by the English Sale of Goods Act, 1893. Necessaries, in every case, mean goods suitable to the condition of life of such

<sup>1</sup> Sections 19 & 20 of the Indian Limitation Act

~~interest and to his actual requirements at the time of delivery.~~ What are necessaries is decided in every case by the court after an inquiry into all the circumstances of the case, such as ~~as to~~ stated, the requirements and other things concerning the minor. In *Nash v. Inman*<sup>1</sup>, the facts were as follows :

A tailor supplied an undergraduate of Cambridge who was an infant, with a few velvet suits. The father of the undergraduate deposed that at the time his son was amply provided with such suits. The Court held that the suits supplied were not to be considered necessaries as there was no need for them at the time in question, and, therefore, the minor was held not liable to pay for them. An infant was also similarly liable to pay a reasonable sum for his education or for instructions in a trade suitable to his conditions in life and he was also bound by a contract to serve for wages, provided it was, as a whole, for his benefit at the time when it was made.

But after the passing of the Infants Relief Act, 1874, an infant's contracts in England are now divided into three classes : (1) Void, (2) Voidable and (3) Valid.

(1) *Void* : Under the Act the following three classes of contracts have been declared absolutely void :

- (a) Contracts for re-payment of money lent or to be lent.
- (b) Contracts for goods supplied or to be supplied excepting necessities, and
- (c) Contracts on accounts stated.

(2) *Voidable* : There are certain contracts which are valid and binding on the minor until he avoids it, either during his minority or within a reasonable time after the attainment of majority. These are contracts which relate to sale or lease of immoveable properties and partnerships.

(3) *Valid* : As by common law, so also under the Act an infant can enter into a valid contract for necessaries and for his benefit.

According to Indian law the age of majority is now regulated by the Indian Majority Act of 1875. According to Indian Law, to the Act, every person shall be deemed to have attained majority when he shall have completed the age of 18 years, and not before. In the case, however, of a minor of whose

person or property or both a guardian has been appointed by a Court, or of whose property the superintendence is assumed by a Court of Wards, before the minor has attained the age of 18 years, the Act provides that the age of majority shall be deemed to have been attained on the minor completing his age of 21 years. According to the Indian law, a person who has not attained majority is called a minor and not an infant, -which is the term used in English law.

Unlike English law, the Indian Contract Act<sup>1</sup>, declares that all contracts by minors are absolutely void excepting contracts for necessities and for his benefit. This is confirmed by the decision of the Judicial Committee of the Privy Council in 'the case of Mohor Bibi vs Dharundas'. Exception, however, to this rule is provided by contracts for necessities and for the benefit of the minor, in respect of which the law is the same as in England, excepting for one fundamental difference. The difference is that while in England under such contracts the minor is personally liable, in India it is not the minor but his estate which is liable.

Certain rules of exception have, however, to be noted in addition to what has been referred to above. Firstly, though a minor cannot enter into a valid contract excepting for necessities and for his benefit, yet an agreement entered into by a competent person on his behalf can be validly enforced by him and against him. Thus a minor's property can be sold or leased out by his guardian and the minor, in all such cases, is bound by it unless, of course, it is proved that the guardian was acting adversely to the interest of the minor. Secondly, according to some decisions of the Allahabad and Madras High Courts it has been held that, if a minor makes a contract by fraudulently representing to the other party that he has attained majority, he may be estopped by Section 115 of the Indian Evidence Act from setting up that he was a minor when he entered into the contract. But the Calcutta High Court tends to incline to the view that the doctrine of Estoppel does not affect Section 10 of the Indian Contract Act, whereby all contracts of a minor have been declared void excepting the cases already referred to. It seems that the Calcutta High Court is right, for, in a body of codified law as in enactment

<sup>1</sup> Section 10

<sup>2</sup> 30 Cal 579

<sup>3</sup> For details re S 115 of the Evidence Act see *infra*

should be so construed as to render the express provision of another instrument absolutely nugatory. This view is confirmed by the decision of the Lahore High Court in *Khangul vs Lalha Singh*<sup>1</sup>.

### **Contracts by persons of unsound mind :**

(b) Lunatics and drunken persons are generally regarded as persons of unsound mind. Contracts entered into by a person during his lunacy or drunkenness are void. But a contract entered into by a lunatic when he is sane and sober and is perfectly capable of forming a rational judgment on the contract, is valid.

### **2. Free Consent :**

Two or more persons are said to consent when they agree upon the same thing in the same sense. A agreed to buy of B 125 bales of Surat Cotton to arrive *ex Peerless* sailing from Bombay. There were two ships named *Peerless* sailing from Bombay and A had in his mind one of these ships B the other. It was held that there was no contract as the parties did not agree upon *the same thing*, in the same sense. A consent is said to be not free when it is caused by any one of the following:

- (A) Coercion, (B) Undue influence (C) Mistake (D) Misrepresentation and (E) Fraud

#### **(A) Coercion :**

An agreement is said to be induced by coercion when one party compel the other to enter into the agreement by (i) committing or threatening to commit an act punishable by the Indian Penal Code or (ii) detaining or threatening to detain unlawfully any property to the prejudice of any person<sup>1</sup>. A says to B, 'I shall set fire to your house unless you agree to sell the house to me for Rs 1000'. B says, 'All right I shall sell you my house for Rs 1000'. This is obviously an agreement caused by coercion and A will not be allowed to enforce the agreement again B. B has the right to treat the contract as void. But if B finds it profitable to sell the house, he can compel A to perform the contract. The person using coercion has no right on

<sup>1</sup> (1921) 9 Lah 701

<sup>2</sup> See *Lion* 13

<sup>3</sup> *R v. Me v. Michelham* (1864) H & C, 906

<sup>4</sup> Section 1

the contract. But the person coerced has the right to treat the contract either as void or as binding. Contracts induced by coercion are thus voidable at the instance of the person coerced.

It should be noted that it is immaterial whether the Indian Penal Code is or is not in force in the place where the coercion is employed. The following example given by the Indian Contract Act<sup>1</sup> will make it clear:

A, on board an English ship on the high seas, causes B to enter into an agreement by an act amounting to criminal intemidation under the Indian Penal Code. A afterwards sues B for breach of contract in Calcutta. A has employed coercion, although his act is not an offence by the law of England and although sec 506 of the Indian Penal Code was not in force at the time when or place where the act was done.

### (B) Undue Influence :

A contract is said to be induced by undue influence where the relations subsisting between the parties are such that one of the parties is in a position to dominate the will of the other and uses that position to obtain an unfair advantage over the other.

Dominion over the will of another is inferred in the following circumstances:

- (i) Where a party holds real or apparent authority over the other, e.g., a father in relation to his child.
- (ii) Where a party stands in a fiduciary relation to the other, e.g., a solicitor in relation to his client.
- (iii) Where a person makes a contract with a person whose mental capacity is temporarily or permanently affected by reason of age, illness or mental or bodily distress, e.g., a doctor entering into contract with his patient.

All contracts induced by undue influence are voidable at the option of the party over whom the undue influence is exercised. Where such a relationship exists between the parties as would normally lead to the inference that one party is in a position to dominate the will of the other, the next question to be decided is whether the contract is unfair for the latter. If it is unfair,

<sup>1</sup> Sec 15

the presumption will be that the contract was caused by the exercise of undue influence. The burden of proving that no such influence was exercised will rest on the former. The following examples will clearly illustrate contracts brought about by the exercise of undue influence.

- (a) A having advanced money to B, his son during his minority, upon B's coming of age obtains, by misuse of parental influence a bond from B for a greater amount than the sum due in respect of the advance. A employs undue influence.
- (b) A, a man enfeebled by disease or age is induced by B's influence over him as his medical attendant to agree to pay B an unreasonable sum for his professional services. B employs undue influence.

There are cases however which should be carefully distinguished from cases of undue influence.

- (c) Thus A applies to a banker for a loan at a time when money is very scarce. The banker declines to give the loan except at an unusually high rate of interest. A accepts the loan on these terms. This is a transaction in the ordinary course of business, and the contract is not induced by undue influence.

#### (C) Mistake :

Where both the parties to an agreement are under a mistake as to a matter of fact essential to the agreement, the agreement is void<sup>1</sup>. Mistake nullifies consent but only when the following conditions are satisfied:

- (i) Both the parties are suffering from the mistake. Mistake on the part of one of the parties only does not make a contract void. If A purchases B's horse for £500/- thinking that it had won the Derby race without B ever having induced the belief, the contract will not be void. The mistake was only unilateral.
- (ii) The mistake must be as to an essential fact. Mere mistake as to any important particular, or any collateral circumstances or mistakes of judgment or value will not make a contract void. The following

may be cited as instances of mistake as to an essential fact of the contract.

- (a) The parties may be mistaken as to the identity of the contracting parties. A lady comes to a jeweller's shop and represents herself as Mrs X. If the jeweller contracts to sell any jewel to the lady the contract will be void from the very outset as the contract is purporting to be between the jeweller and Mrs X and not the lady<sup>1</sup>
- (b) The parties may be mistaken as to the identity of the subject matter about which they are apparently agreeing. A agreed to buy from B Surat Cotton to arrive at Peerless from Bombay". There were two ships named *Peerless* sailing from Bombay and A had in his mind one of these ships, B the other. It was held that as there was a mistake as to the identity of the subject matter of the supposed contract there was no contract at all.

If the mistake is as to the quality of the thing contracted for, the mistake will only affect consent if it is a mistake of both parties and is as to the existence of some quality which makes the thing without the quality essentially different from the thing as it was believed to be. A common mistake as to some quality which only makes the thing more or less valuable than it was supposed to be will not invalidate the contract. A buys a picture which both the buyer and the seller believe to be the work of an old master. The buyer pays a high price. It turns out that the picture is only a modern copy. The contract will stand in the absence of misrepresentation<sup>2</sup>.

- (c) The parties may be mistaken as to the basis of the contract. Thus, if the parties enter into a contract for the sale of some specific article, the existence of that article is the foundation of the contract. If it turns out that the article had perished before the contract, it will be void.

#### (D) Misrepresentation and Fraud :

We have seen above that a mistake makes a contract void.

<sup>1</sup> *Lake vs. Symmons*, (1927) A.C. 487 (For fuller discussion, see post).

<sup>2</sup> *Raffles v. Witchelhaus*, (1864) H & C, 906

<sup>3</sup> See Misrepresentation, infra p. 26

Such mistake is common to both the parties. It is not induced by one to mislead the other. But it is not uncommon to find one party inducing the other to enter into the contract by making a false statement which he himself may believe or disbelieve. A says to B that his horse is healthy and that B might have it for £50/. B relying on the statement of A that his horse is healthy buys the horse for £50. It turns out that the horse is not healthy. If A himself believed that the horse was healthy it will be a case of innocent misrepresentation. If he did not believe so, it will be a case of fraudulent misrepresentation or fraud. In both cases B is entitled to treat the contract as not binding on him, i.e., the contract is voidable at the option of B. If he has not paid the purchase price he can refuse to pay it and ask A to take the horse back. If he has paid the price, he can ask A to take his horse back and refund the purchase money. Let us treat Misrepresentation and Fraud separately. It should, however, be noted that a fraud or misrepresentation which did not cause the consent to a contract of the party on whom such fraud was practised or to whom such misrepresentation was made, does not render a contract voidable!

### **Fraud :**

Section 17 of the Contract Act states that Fraud means and includes any of the following acts committed by a party to a contract, or his agent, with intent to deceive another party or to induce him to enter into the contract.

(1) The suggestion as a fact, of that which is not true by one who does not believe it to be true. A tells B knowing it to be false that his colt is of pure Arab breed. On this suggestion B agrees to buy the colt for Rs. 500. The contract is voidable at the option of B on account of fraud.

(2) The active concealment of a fact by one having knowledge or belief of the fact. It is fraud for one to conceal material facts which he is under an obligation to disclose when he is entering into a contract with another. This duty to disclose does not arise in cases of all contracts. It arises only in the following cases.

(i) Statutory obligation to disclose :—Certain statutory provisions require parties to a contract to make dis-

closure of material facts. Thus, Section 55 of the Transfer of Property Act requires a seller of real property to disclose all defects as to his title or property to the buyer. Therefore, if in contravention of this provision the seller conceals any defect in his title and tells the buyer that his property is free from all incumbrances, the buyer may treat the contract as void even if he buys the property, in case the property turns out to be mortgaged or subject to similar incumbrances.

- (ii) **Duty to disclose arising out of *Uberrimae fidei*** (utmost abundant faith) - When parties to a contract stand in such a relationship that utmost good faith is required of them, they must disclose all material facts. Family settlements or compromise of disputes contracts between solicitors and clients, or between doctors and patients, or between father and son, or between trustee and *cestui que trust* are illustrations of contracts of this type wherein the parties must disclose all material facts.

**Duty to disclose material facts in contracts of insurance, e.g., Life Assurance or Fire and Marine Insurances,** is also imposed on the party assured by the Insurance Act. The reason for this is that only the assured knows all facts relating to the risk undertaken by the Insurance company e.g., details about illness, age and so on of the party assured. If the material facts are not disclosed, the company is entitled to treat the policy as void.

In all other cases of contract where there is no duty to disclose cast on the parties, the parties must take care of themselves. Thus, in ordinary contracts of sale the buyer must be care of himself. The seller is under no obligation to disclose material facts. A sells his horse to B for £50. A knew that the horse was ill. But he never made any representation to B to the effect that his horse was not ill. His concealment of his horse's illness will give B no ground to treat the contract as void, for A had no duty to disclose material facts. B ought to have verified facts for himself. This is what is known as *Caveat Emptor, i.e., "buyer beware."*

(3) **A promise made without my intention of performing it;** —If a party to a contract makes a promise, which he has no intention of performing, with a view to inducing the other party

to enter into the contract, he commits fraud. B gives A Rs. 100/- on A's promise to draw a portrait for him. A has no intention to draw the portrait. A is guilty of fraud.

(4)) Any act or omission which the law specially declares to be fraudulent :—Certain statutes declare certain acts as fraudulent. Thus, any transfer of immovable property made with intent to defraud creditors is declared fraudulent by the Transfer of Property Act.

(5) Any other act fitted to deceive.

(6) Silence as Fraud :—Merely silence as to facts likely to affect the willingness of a person to enter into a contract is not fraud, unless the circumstances of the case are such that, regard being had to them, it is the duty of the person keeping silent to speak, or unless his silence is, in itself, equivalent to speech. B says to A—' If you do not deny it, I shall assume that the horse is sound.' A says nothing. Here A's silence is equivalent to speech. If in this case B buys the horse and finds that the horse is unsound, he can impeach the contract for fraud which in this case was A's silence.

### **Misrepresentation :**

We have seen before what is the essence of misrepresentation. Misrepresentation means and includes -

(1) The positive assertion, in a manner not warranted by the information of the person making it, of that which is not

Section 18 true, though he believes it to be true. A tells B that his land produces 1000 bushels of wheat.

On that representation B buys the land. It turns out that the land produces only 400 bushels of wheat. But A believed that it produced 1000 bushels of wheat though he had no reason to believe so on the information he had. B can treat the contract as void for misrepresentation. But if *A had good reasons to believe in his statement on the information he had, it would not have been a case of misrepresentation*. It would have been a case of mutual mistake.

(2) Any breach of duty which, without an intent to deceive, gains an advantage to the person committing it, or any one claiming under him, by misleading another to his prejudice or to the prejudice of anyone claiming under him. We have seen before that in a contract of insurance the person assured has a

duty to disclose his age etc. If the assured on an honest belief states his age as 25 whereas he is really 27 and thereby obtains a lower premium, it will be a case of misrepresentation by breach of duty without an intent to deceive.

(3) Causing however innocently, a party to an agreement to make a mistake as to the substance of the thing which is the subject of the agreement. Mistake induced by one party to the contract as to the main subject matter of the contract makes the contract voidable at the option of the other party even if that inducement was innocent. Mistake about any particular matter not forming by itself the subject matter of the contract will only amount to a breach of warranty<sup>1</sup> but not to misrepresentation. A says to B 'My house is free of any defect.' B buys the house. A did not know that there was a severe crack in the foundation of the house the existence of which makes living in the house dangerous. If and when B finds out the defect, he can treat the contract as void for misrepresentation as the defect vitally affects the house which is the subject matter of the contract. If, however instead of the defect above mentioned only one window is broken B could not have treated the contract as void, for the break in window is not one which vitally affects the subject matter of the contract. It would only amount to breach of warranty.

*Effect of Misrepresentation and Fraud.* The effect of both misrepresentation and fraud is that the party on whom fraud has been practised or to whom misrepresentation has been made, can either treat the contract as void or compel the other party to perform his part of the contract. In case of fraud the party injured is entitled to damages for fraud over and above his remedy of treating the contract as void.

#### **Void, Voidable and Unenforceable Contract :**

A contract is said to be void when what is alleged to be the contract does not confer any right or impose any obligation on either party. It is, therefore, a little illogical to talk of void contracts.

Void contracts for what is supposed to be the contract is no contract at all. It is however, conveniently used to describe those cases where there is an apparent contract, but it will not have any legal effect either because some essential

<sup>1</sup> For discussion of Warranty see *saya* under Sale of Goods

is lacking or because it is vitiated by being contrary to some law or public policy.

A void contract should be distinguished from an illegal contract. Both are void and unenforceable, but in the case of an illegal contract collateral transactions connected with the main contract are vitiated, whereas in the case of void contracts, collateral transactions are not affected at all. Thus, if I advance a man money to enable him to purchase enemy goods, I cannot recover the money. A contract to buy enemy goods is illegal. My advance was collateral to this main illegal contract. Therefore, though advancing money as a loan is a valid contract, yet in this case it is void, as it is collateral to an illegal contract. But if I advanced the money to enable the man to bet on a horse race, I could have recovered the money. Betting on a horse race is void but not illegal. Therefore this advance is collateral to a void contract and not to my illegal contract and is such can be recovered.

A contract may be void due to mistake, illegality of its object or such object being contrary to the public policy and incapacity of the parties, and so on.

**A voidable contract** is one which one party has a right to treat as void if he so chooses but it is valid unless and until he does so treat it as void. The most common example of a voidable contract is one where one of the parties has been induced to enter into an agreement by misrepresentation or fraud. Thus, if A fraudulently represents himself to be a big businessman and induces B to sell him certain goods and to give him delivery on credit, B may, if he so chooses, void the contract which he was induced to enter into by fraud. But until and unless B so exercises his option, any bona fide purchaser who buys the goods from A without notice of the fraud, will acquire a good title over the goods.<sup>1</sup> This brings to sharp relief the distinction between a void and voidable contract. For if in the above case B delivers the goods under a mistaken belief that A is Lord Halifax, and A sells these goods to D, a bona fide purchaser for value without notice, D will have no title to the goods and B can still recover the goods from him. The reason is that the contract between A and B was void from the

<sup>1</sup> *Phillips v. Brooks* (1919) 2 K.B. 243

very start due to a mistake as to the identity of the parties, and, therefore, A had never any title over the goods which he purported to sell to D<sup>1</sup>. In the first case there is a contract until avoided by the party entitled to avoid it. In the second case there has never been any contract at all and neither party had any right or obligation under it.

According to Section 10 of the Indian Contract Act all agreements are contracts if they are made by the parties competent to contract, for a lawful consideration and with a lawful object. This means that an agreement becomes a contract when these conditions are satisfied.

But even where all these conditions are satisfied under certain circumstances, the courts will not enforce contracts otherwise valid. These are (1) a contract made on account of natural love and affection between parties standing in a near relation to each other will not be enforced unless it is in writing and registered, (2) a contract made between persons whereby one agrees to repay a time barred debt which was originally due to the other will not be enforced unless it is in writing and signed by the party making the promise or by his duly authorised agent and (3) a contract between parties to refer their present or future disputes to arbitration will not be enforced unless it is made in writing. (4) Contracts made by companies will not be enforced unless it is made in writing. (5) By the Law of Property Act all mortgages other than equitable mortgages where the principal money secured is Rs 10/- or upward, and gift of immovable property must be made in writing and registered in default they will not be enforced.

### **Void Contracts :**

A contract becomes void in the following cases:

(i) *Mistake* - We have seen before how different types of mistakes render a contract void *ab initio*.

(ii) *Illegality of promise or consideration* - Illegality makes a contract void. A contract is illegal if the consideration or the promise involves doing something illegal or contrary to public policy. A says to B "I shall pay you Rs 500 if you murder C". Here, there cannot be any valid agreement as the consideration

<sup>1</sup> *Cundis v. Landra* (1879) 3 AC 459

<sup>2</sup> Section 24

of A's payment of Rs. 500 is B's act of committing a murder, which is illegal.

(m) *Illegality of object*<sup>1</sup> Object of contract means the purpose for which the contract is entered into. Now it may quite happen that the object of a contract is unlawful, whereas its consideration is lawful. A takes the lease of a house belonging to B for Rs. 50 a month. There is nothing unlawful in it<sup>2</sup>. But A intends to use the house to hold seditious meetings. The contract is unlawful and void as the object of the contract is unlawful.

The following may be regarded as unlawful objects -

(a) When the object of an agreement is in contravention of any statute, or opposed to the provisions and intent of any Act, it becomes illegal. It is unlawful for a person to draw Hundis on himself payable to bearer on demand according to S. 31 of the Reserve Bank Act. If any one contracts to draw such Hundis in contravention of this Act, the contract will be illegal and void.

(b) A contract with the object of defrauding others is illegal and void. P has a patent right for a certain process in England. B enters into a contract with P for securing the sole agency for working the process in Berlin. B knew he could not exercise this sole agency right in Germany. The object of the contract was to induce share holders to buy shares in a company by representing that B had the right contracted for. As the object of the contract was to defraud share holders, the contract was illegal and void. *Bengal vs. Phosphite Sewage Co.*<sup>3</sup>

(iv) *Object contrary to public policy* Contracts having as their purpose objects which are contrary to public policy are void because they are looked on by courts of law with disfavour as being detrimental to public welfare and morals.

(v) *Agreement in restraint of marriage* Any contract which has as its object the restraint of any adult person from marrying is void as being against public policy.<sup>4</sup>

(vi) *Agreement in restraint of legal proceedings* Any agreement purporting to take away from any person his right to seek

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<sup>1</sup> Sec. 23

<sup>2</sup> Ibid

(1875) L.R. 10 Q.B. 449

<sup>4</sup> Section 26

remedy in a court of law is void. An agreement to refer disputes to arbitration is not, however, void.<sup>1</sup>

(iii) *Agreement in restraint of trade -*

Agreements in restraint of trade are generally one of the following varieties:

(a) Agreements restraining a party to a contract from pursuing his occupation after termination of partnership or apprenticeship articles or contracts of service.

(b) Agreements restraining a person selling the goodwill of his business from carrying on a similar competitive business.

(c) Agreements by which the persons voluntarily curb their rights to regulate the prices or the mode of carrying on their business by entering into a joint agreement amongst themselves. Such agreements are illustrated by the formation of Syndicates or Trusts like the Bengal Bus Syndicate.

(d) Agreements by workmen to regulate their wages and their conditions of work by Trade Unions set up by themselves.

Even as late as in the reign of Queen Elizabeth all restraints of trade whether general or partial for whatever purpose, were held to be contrary to public policy and therefore, English law void. In course of time however with the growth of industry and trade as a result of industrial and commercial revolution, it was found that certain restraints of trade were necessary and that it would interfere with very dry transactions if such restraints could not be imposed. It is to reason that nobody would buy the goodwill of a business unless he had the right to restrain the seller from setting up a competing business under the same name subsequently, nor would an employer desire to employ a person in a position where he would know all the secrets of the business of his master unless the master had the right of protecting himself against his employee's use of the secrets he had learnt after the employee had left his master's employment. Hence the law in England regarding restraints of trade has been relaxed considerably in recent times and any restraint of trade, which is reasonable having regard to the interests of both the parties and is not injurious to the public, is valid. In all cases the court decides the question of reasonableness by

<sup>1</sup> Section 28

- *Calgate vs. Bachelor* (1902) Cro. Eliz. 52

reference to the nature of the business, trade or occupation, the area over which the restraint is to be imposed and the length of time for which it is to continue. The wider the area or the longer the time over or during which the restraint is to operate, the more difficult it is to justify the reasonableness of the restraint. As regards contracts between the vendors and purchasers of a business or agreements for the maintenance of prices or regulation of business relations between traders, the law regards the parties as best judges of what is reasonable as between themselves and unless a restraint in this sphere extends over too long a period or too wide in area, having regard to all the circumstances, the Court will be loath to declare the restraint invalid simply because it may involve some injury to the public. But in regard to contracts between a master and a servant the law is different. In *Nordenfeldt v. Maxim Nordenfeldt Gun Co.*<sup>1</sup> it was pointed out by Lord Macnaghten that who ever is the purchaser of a business is entitled to impose restraints protecting himself against the vendor's future competition. A master is not entitled to protect himself if all he fears competition of his servant. A master can only impose such restraint on his servant as is necessary to protect him from the use by the servant, in a confidential position, of trade secrets, names of customers and other information confidentially obtained. But he cannot restrain the servant from using his personal skill and knowledge which he has himself acquired. In *Morris v. Sixelby*, Sixelby was employed by Morris Limited as draughtsman and covenanted that he would not, for seven years after leaving their employment carry on business anywhere in the United Kingdom in the sale of various kinds of machinery. A year after leaving his employment, he entered into the employment of a competing firm at Manchester. The House of Lords held that the restraint was bad in as much as the servant was sought to be restrained from making use of his personal skill which is contrary to public policy.

In India by Section 27 of the Indian Contract Act, however, *Indian Law* in agreement by which income is restrained from using a lawful profession, trade or business of any kind is to that extent void. But the following exceptions are recognised:

<sup>1</sup> (1904) A.C. 545

<sup>2</sup> (1916) I A.C. 68

(1) One who sells the goodwill of a business may agree with the buyer to refrain from carrying on a similar business within specified local limits, so long as the buyer or any other person deriving title to the goodwill from him carries on a like business therein, provided that such limits appear to the Court reasonable, regard being had to the nature of the business.

(2) Partners may, upon or in anticipation of a dissolution of partnership, agree that some or all of them will not carry on a business similar to that of the partnership within such local limits, as might appear to the Court to be reasonable, regard being had to the nature of the business.

(3) Partners may agree that some one or all of them will not carry on any business other than that of the partnership during the continuance of the partnership.

(4) By implication a contract of service entered into by a person to serve another for a fixed period restrains him from serving anyone else during that period. Such restraints by implications are valid, otherwise a contract of service would be of no effect.

(5) An agreement to sell goods necessarily implies that the vendor is restrained from selling it to any one else except the purchaser. Such a restraint is valid; otherwise an agreement to sell would be of no effect.

It appears, therefore, that in India all restraints on trade excepting the cases mentioned above are void. It does not matter whether the restraint is partial or general or is reasonable. Unless a contract in restraint of trade can be brought within the exceptions indicated above, it will be void. In this respect it differs from the law in England which has been sketched above. Thus in *Madhab Ch. vs. Raj Coomar Das*<sup>1</sup> the parties carried on business as braziers in a certain part of Calcutta. The plaintiff's mode of business was found by the defendants to be detrimental to their interests, and an arrangement was thereupon entered into between the parties whereby the plaintiff agreed to stop his business in that quarter and the defendants promised, in consideration of his doing so, to pay to the plaintiff all sums which he had then paid as advance to workmen. The plaintiff accordingly ceased carrying on business in that locality and the

defendants having failed to perform their part of the contract, he sued them to recover Rs 900/- being the amount advanced by him to the workmen. The agreement was held void under Section 27, though the restriction put on the plaintiff's business was limited to particular place and seemed quite reasonable. As a whole the agreement was void and there was no consideration for the agreement on the part of the defendant to pay the money and the whole contract was held to be unenforceable. This case illustrates the great difference between the Indian and the English law on the subject.

(iii) *Contracts by way of wager*

In *Caulill vs Carbolic Smoke Ball Co*<sup>1</sup> Hawkins, J. defined a contract by way of wager as follows: 'A wagering contract is one by which two persons, professing to hold opposite views touching the issue of a future uncertain event, mutually agree that, dependent on the determination of that event, one shall win from the other, and that other shall pay or hand over to him a sum of money or other stake neither of the contracting parties having any other interests in that contract than the sum or stake he will so win or lose, there being, no other real consideration for the making of such contracts by either of the parties.' It is essential to a wagering contract that each party may under it either win or lose, whether he will win or lose being dependent on the issue of the event and therefore remaining uncertain until that issue is known. If either of the parties may win but cannot lose, or may lose but cannot win, it is not a wagering contract. Thus if A contracts with B to the effect that A would pay to B, Rs. 50/- if the horse X wins in the race and B would pay A Rs. 50/- if the horse Y fails to win in the race the contract is a typical example of a wager. A will win in the event of X losing in the race. B will win in the event of X winning in the race.

According to Section 37 of the Indian Contract Act an agreement by way of wager is void and no suit can be brought for recovering anything alleged to have been won in any wager and entrusted to any person to abide the result of any game or other uncertain event on which my wager is made. Wagering contracts are not generally illegal and have been declared void only by the Indian

Contract Act. But the Indian Penal Code (S. 294 A) makes it a criminal offence by declaring that whoever keeps any office or place for the purpose of drawing any lottery not authorised by Government shall be punished with imprisonment of either description for a term which may extend to six months or with fine, or both. And whosoever publishes any proposal to pay any sum, or to deliver any goods, or to do or forbear from doing anything for the benefit of any person, on any event or contingency relative or applicable to the drawing of any ticket, lot, number or figure in any such lottery, shall be punished with fine which may extend to Rs. 1,000/- Apart from this type of agreement there is no law in India which makes wagering as such illegal, excepting that they are always void.

A contract of insurance on the other hand is not a wager because the party insured has an interest apart from the wager. Thus, in a contract of fire insurance, the insured's object is to be able to indemnify himself in case he suffers loss due to fire. In the same way, in a contract of life insurance the object of the insured is to secure a compensation for his dependants in the event of his death. A bona fide insurance contract is not a wager. But an insurance on the life of a person in which the insured has no interest whatever is void as being a wager.

#### **Immoral agreement :**

Any agreement for *future illicit cohabitation* or for furtherance of immoral purposes like prostitution is void. A and B agree to live together in illicit cohabitation and A binds himself to pay B £60 annually after his death. The agreement is void<sup>1</sup>. A, a brougham driver, agrees to take B a prostitute, round the town for a certain sum of money so that the latter can attract customers. The contract between A and B is void as against public policy.<sup>2</sup>

#### **Contracts in abuse of legal process :**

A person is entitled to advance money to assist a bona fide litigant. But if the contract for advance of money was for the purpose of stirring up litigation and strife or sharing the profits of litigation or for any other unconscionable purpose, the contract is void as contrary to public policy.

<sup>1</sup> *Walker v. Perkins* (1764) 1 W.Bd. 517

<sup>2</sup> *Pearce v. Brooks* (1866) L.R. 1 Ex. 113

### 'Contracts void for incapacity of parties :

We have seen before that infants, lunatics and insolvents cannot enter into valid contracts.

### Joint liability and joint and several liability :

When two or more persons make a joint promise, the promisee may, in the absence of express agreement to the contrary, compel any one of such joint promisors to perform the whole of the promise (S 43). In this respect Indian Law differs from English Law in that according to English law joint contractors cannot be sued separately but must be sued jointly.

If the promisee obtains damage against one of the joint promisors the other joint promisors must contribute equally with the first joint promisor.

Where the promisee obtains damage for breach of contract against one of the joint promisors and the damage is not realised from him, the promisee cannot sue the other joint promisors for the satisfaction of the damage.

"But a joint promise differs from a joint and several promise. In the case of a joint promise the obligation is single and is extinguished by a judgment recovered in suit against any one of the joint promisors and even if that judgment remains unsatisfied a fresh suit cannot be brought against the other co-promisors." But in the case of joint and several liability the liability is joint as well as separate. Therefore the obligation in this case is not extinguished by recovering judgment against one of the several joint promisors. The creditor can sue more than one joint promisor in case the judgment remains unsatisfied.

### Discharge or termination of contract :

A contract we have seen involves a promisor and a promisee. The promisor and the promisee each creates into certain obligations. When these obligations come to an end, it is said that the contract has been discharged or terminated. Now a contract may be discharged in any one the following ways —

1. By performance or fulfillment<sup>1</sup>
2. By fresh agreement
3. By impossibility of performance<sup>2</sup>

<sup>1</sup> Sections 37, 38, 51, 55

<sup>2</sup> Section 62

<sup>3</sup> Section 56

- 4 By breach or renunciation of contract
- 5 By operation of rules of law

### **Discharge by performance :**

Performance is the most common way of discharging contractual liability. A promises to deliver to B 10 tons of coal if B pays Rs 30/. So far as A is concerned his contractual liability will be discharged when he delivers the ten tons of coal to B in as much as he will be deemed to have performed his side of the contract. Now, a contract involves a double liability. In our above example the first liability is that of A to deliver ten tons of coal. The second liability is that of B to pay Rs 30/. The delivery of coal by A will not naturally discharge B's liability to pay. B's liability will be discharged when he pays Rs 0/. We must therefore distinguish between performance which discharges one of the two parties from his liabilities under a contract and performance which discharges the contract as a whole. When for instance A promises to repair B's watch in consideration of B having mended A's car 3 years ago, the whole contract will be discharged when A repairs B's watch. But where a promise is given in consideration of another, as in our first illustration performance by one party does no more than discharge him who has performed his part.

In a contract where the special skill and personal qualifications of the promisor are the essential parts of performance, the contract performance must be by the promisor himself. In the case of a contract not involving peculiar personal qualifications, the promisor may rely on the act of his agents in performance by himself. Thus if a painter contracts with me to paint my portrait, the painter must paint the portrait himself, for his personal skill and qualifications were what I bargained for. He cannot rely on another painter to do the job. But if I have a contract with a grocer to supply me with Rs 5/- worth of sugar and tea every week, it matters not to me from whom the sugar and tea might come so long as they are of the same quality as I bargained for. The grocer may perform his side of the contract very well by relying on another

grocer or any other agent of his for the supply of the things to me.<sup>1</sup>

Where according to the contract the promisor is to perform his promise without the promisee asking him to do it, i.e., without application by the promisee, and no time for performance is specified, the contract must be performed within a reasonable time<sup>2</sup>. What is a reasonable time depends in each case on all the facts and circumstances of the case. One day may be reasonable in the case of a contract for sale of shares, whereas 1 year may not be unreasonable in a contract for sale of land. When a promise is to be performed on a certain day, and the promisor has undertaken to perform it without application by the promisee, the promisor may perform it at any time during the usual hours of business on such day and at the place at which the promise ought to be performed<sup>3</sup>. When a promise is to be performed on a certain day and the promisor has not undertaken to perform it without application by the promisee, it is the duty of the promisee to apply for performance at a proper place and within the usual hours of business. When a promise is to be performed without application by the promisee and no place is fixed for the performance of it, the promisor should apply to the promisee to appoint a reasonable place for the performance of the promise and to perform it at such place<sup>4</sup>.

#### **Time being the essence of contract :**

When a party to a contract promises to do a thing at or before a specified time and fails to perform the contract at or before the specified time, the promisee can treat the contract as void, i.e., avoid the contract, only if it was the intention of the parties that time should be the essence of the contract.

If it was not the intention of the parties that time should be the essence of the contract, the contract does not become voidable by the failure of the promisor to perform the contract at or before the specified time<sup>5</sup>.

<sup>1</sup> Section 40.

<sup>2</sup> Section 46.

<sup>3</sup> Section 47.

<sup>4</sup> Section 48.

<sup>5</sup> Section 49.

<sup>6</sup> Section 55.

The intention of the parties to make time the essence of the contract may be gathered from express word or from the nature of the transaction.

In mercantile transactions time is usually deemed to be the essence of contract unless otherwise provided. But in the case of sale of land, time is not regarded as the essence unless otherwise provided.

## 2. Discharge by fresh agreement :

The parties to a contract may, by a fresh agreement, discharge the old contract. This can be done in three ways, namely

(a) *Recession*, (b) *Alteration* and (c) *Novation*.

(a) *Recession* Recession simply means rescinding or cancelling the original contract by mutual agreement whereby the old contract ceases to be binding on any of the parties.

(b) *Alteration* Alteration means substituting a fresh contract with altered or different terms from the original one. A agrees to supply B 500 yard of blue serge for Rs 6 a yard within 6 months. Later on A will alter the agreement in the following way. A agrees to supply 400 yards instead of 500 yard within eight months instead of six. The latter agreement puts an end to the former.

(c) *Novation* Novation takes place when one party to a contract releases the other in exchange to the contract comes and accepts the liability of the party released. In a novation actually means a new agreement which substitutes the old one wherein (i) one of the parties to the original contract is relieved of all liabilities and (ii) a new party undertakes all the liabilities of the relieved party in consideration for the release. Miller's case<sup>1</sup> gives us an example of novation. The facts were as follows. A particular Insurance Company agreed to pay Miller's heirs an annuity of £200/- on his death in consideration of Miller paying a certain annual premium. Later on, the European Association took over the business of the Insurance Co. It was agreed that the European Association will be bound by all the contracts of the Insurance Co. Miller also agreed to this arrangement and started paying his premium to the European Association. It was a case of novation and the contract between Miller and the Insurance Co. was discharged.

### 3. Discharge by impossibility of performance :

It is a well known fact that an agreement to do the impossible is by itself void<sup>1</sup>. If I agree with B to take him to the moon for a certain sum, the agreement will be void *ab initio*. But it happens very often that parties to a contract undertake to do certain things which are by no means impossible but which become impossible to perform later on due to causes beyond their control. This is called *supervening impossibility*. In such a case the contract is discharged and becomes void.

#### **Supervening impossibility :**

Supervening impossibility arises in the following ways:

(a) Impossibility arising due to change of law. One cannot agree to do a thing illegal at the time of the contract, but if one contracts to do a thing which is, at the time of the contract, lawful, but a new Act comes in and hinders him from doing it, the contract will be discharged. In *Karsell v. Timbe Operators and Contractors*, there was an agreement for the supply of timber from Latvian forests. By a subsequent Latvian Law the cutting of timber by private companies was forbidden. The party which was bound by the contract to supply such timber was excused and the contract was held to be discharged by the coming in of the new Latvian law. Similarly a contract to supply goods from a country against which war is subsequently declared will be discharged as it will be illegal to supply such goods.

(b) Impossibility due to the destruction of things or persons vital to the contract. In a contract where performance depends on the continued existence of a given person or specific thing or of the existing state of affairs, the impossibility arising as a result of the destruction of such person or thing will discharge the contract and excuse performance. In *Howell v. Coupland*<sup>2</sup>, the defendant contracted to deliver to the plaintiff part of a specific crop of potatoes in autumn. Before autumn the crop was destroyed by pest due to no fault of the defendant. It was held that the performance of the contract depended upon the existence of the crop. With the destruction of the crop, the contract was

<sup>1</sup> Section 56.

<sup>2</sup> (1927) 1 K.B. 298.

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also discharged. Similarly, in *Taylor v. Caldwell*<sup>1</sup> the defendants agreed to let a music hall to the plaintiff for a series of concerts. Subsequently the music hall was destroyed by fire. It was held that as the existence of the music hall was the foundation of the contract, the contract was discharged with the destruction of the hall.

(e) Impossibility due to non-occurrence of contemplated events or state of things :—Where the happening of a future event or the continued existence of a certain state of things are *contemplated* by the parties as the only *foundation* of the contract, the contract is discharged when the event does not happen or the state of things comes to an end. This is called discharge under a condition. A condition is something on which the whole contract rests. It may be either (i) a condition precedent or (ii) a condition subsequent or (iii) a concurrent condition.

(i) A condition precedent is a condition, *express* or *implied*, that the contract shall not bind one or both of the parties until and unless some event has happened.

A agrees to take the house of B provided the drains are in order. In this case A will not be bound to take the house unless the drains are in order.

(ii) A condition subsequent is a condition *express* or *implied* that upon the happening of some event after the contract has become binding, the contract will be discharged. A takes the lease of B's house for three years with the provision that the lease shall terminate whenever the drains will go out of repair. Here, if after one year the drains get out of repair, A can terminate the lease.

(iii) When in a contract the obligation of each party is dependent on the performance by the other, it is said that the obligation of each is a concurrent condition of the obligation of the other.

In all our previous examples conditions have been expressly mentioned. But the rule regarding them applies to cases where it can be inferred from the terms of the contract and the surrounding circumstances that the happening of a future event or the

<sup>1</sup> (1863) 3 B. & S. 826.

continuance of some state of things must have been contemplated by both the parties as the basis of the contract.

In all such cases where from the terms of the contract and the surrounding circumstances it can be inferred that the happening of some future events or the continuance of some state of things must have been contemplated by both the parties as the basis of the contract, the law will imply that the contract is made subject to a condition subsequent and that it is to be dissolved if that event does not take place or if the state of things changes. This implied condition only excuses the performance if subsequently the whole contract becomes impossible of performance through some cause for which neither party is responsible. This cause must be such as to frustrate either the performance of the contract.

In Kell v. Henry<sup>1</sup> the tenant Henry agreed to hire a flat belonging to Kell on a day on which the Coronation procession of King Edward VII was arranged to pass. Kell's flat was on the path through which the procession would pass. Afterward the procession was delayed on the day originally fixed due to the king's illness. It was held in his favor that the abandonment of the Coronation procession owing to the illness of the king did not upset the performance of the contract as the contract was interpreted to one for the hiring of the flat solely for the purpose of viewing the Coronation procession and is the taking up of the coronation procession was regarded by both the contracting parties as the sole foundation of the contract. This found to having been destroyed the contract was discharged and Henry had no liability regarding the rent of the flat.

#### **Rights of parties in case of discharge by supervening Impossibility :**

According to section 56 of the Indian Contract Act a contract becomes discharged due to supervening impossibility. Where contract becomes impossible due to this cause, it becomes void and the party who has received any advantage under it, is bound to restore it to the other party under Section 55 of the Indian Contract Act. In Boggiano & Co. v. Arab Steamers Co. Ltd. the facts were as follows:

<sup>1</sup>(1903) 2 K.B. 740  
<sup>2</sup>(1916) 40 Bom. 529

A pays freight to B for 2,500 bales of cotton to be carried on a ship belonging to B from Bombay to Genoa. The freight is paid in advance, and the goods are put on board the ship. While the ship is lying in the harbour, export of cotton to Genoa is prohibited by orders of the Government and the voyage is abandoned. A is entitled under section 65 to recover from B the freight paid in advance. This right is not affected even if B is a common carrier. The Privy Council in one of its latest decisions in *Muridhui Chitterjee vs. The International Film Co. Ltd.*<sup>1</sup> has extended the principle of restitution to cases where one party incites a contract for the default of the other. It has been laid down that in such cases the party who incites the contract is entitled to damages if he has suffered any loss but is bound at the same time to restore any advantage which he has received by the contract.

In England however the law is somewhat different to that in India. Those who are contract are absolved by reason of supervening impossibility from liability to the public or excused from further payment to the other party where it lies at the time when the contract is dissolved. The law was laid down in *Chandler v. Webster* as follows:—“(1) when he is paid for money not due at the time of dissolution (2) no action lies to recover back money lawfully paid under the contract before its dissolution (3) money due but unpaid at the time of dissolution is recoverable.” In *the Civil Serv. Co. v. Society Ltd. & General Steam Navigation Co.* the Plaintiff as a charter party agreed to have a time to a Naval Review at the occasion of the King’s Coronation and in accordance with the terms of the Charter party paid £ 20 in advance. The review having taken place and the Plaintiff failing to cover the money paid.

It is obvious from the above that the liabilities of the parties under a contract which is discharged by force of supervening impossibility is different in India from those in England. But in the latest House of Lords decision in *Fibrosa Spolka Akcyjna vs. Fairburn Lissom Combe Bubon, Ltd.*<sup>2</sup> the English Law

<sup>1</sup> 47 CWN 497

<sup>2</sup> (1904) 1 KB 493

<sup>3</sup> (1903) 2 KB 756

<sup>4</sup> (1942) 2 AER 122

has been brought into line with the Indian Law and the old law in *Chandler vs. Webster* has been overruled.

#### **4. Discharge by breach or renunciation :**

Where one party to a contract breaks the contract or shows by his conduct or words unwillingness to carry out his part of the contract, the other party is entitled to treat the contract as discharged. He has two remedies, *viz.*,

- (i) to treat the contract as discharged and to sue the offending party for damage for breach of contract, or
- (ii) to treat the contract as still binding in case the time for the performance of it has not yet arrived and compel the other party to perform his part when the time for it comes.

**N.B.** When one party to a contract shows by conduct or words his unwillingness to perform his part of the contract or is incapacitated in such a way as not to be able to perform, the other party can treat such a conduct as *an anticipatory breach of contract*.

It is called an anticipatory breach because the contract is not broken, but is in all likelihood going to be broken. In such a case, the other party need not wait for the time of the performance of the contract. He can repudiate the contract and treat it as discharged as soon as there is an anticipatory breach.

#### **5. Discharge by operation of law :**

In certain cases contracts are discharged by the operation of certain laws even though such contracts be valid in every respect. Thus, under the Limitation Act certain contracts become discharged after the lapse of a prescribed period of time and parties to such contracts cannot sue on them after the expiry of the prescribed period of time. Similarly, when an insolvent is discharged by the Insolvency Court, all his contracts are discharged by the operation of the Law of Insolvency.

#### **Breach of contract :**

Breaches of contract are of two kinds, either of which gives a cause of action to the party injured by the breach :—

- (1) Actual Breach—This happens when a party does not perform his promise in the manner and at the time stipulated by the contract. B contracts to sell his land to A before 1st

July, 1941. B fails to convey the land before 1st July 1941 B has broken the contract

(2) Anticipatory breach or Breach by renunciation This happens when before the time for performance, a party shows by his conduct or words his unequivocal intention of not performing the contract or makes himself incapable of performing the contract A contracts to build a house for B for a certain sum within two years Even after a year and a half has passed A has not started any work on the house Moreover he has told B's agent several times that he would not start any work on the house unless B agrees to pay him a greater sum than that stipulated in the contract B need not wait till two years have elapsed and then sue B for breach of contract He may at once sue B for breach of contract for the intention of B not to proceed with the contract was manifest and it amounted to renunciation or anticipatory breach of contract

### **Remedies for Breach of Contract :**

In case of a breach of contract the party injured has the following remedies

- (i) He can treat the contract as discharged and not binding on him and claim damages for the breach of contract
- (ii) He can claim a *quantum meruit* i.e. a reasonable sum is recoverable for anything that he might have done under the contract
- (iii) He can claim damages in an action upon the contract

#### **(i) Discharge :**

We have discussed before how breach of contract by one party relieves the other party from all contractual liabilities The injured party can further sue for damages for breach of contract

#### **(ii) Quantum Meruit :**

*Quantum meruit* literally means giving a person as much as he has earned Where a person supplies another person with goods or works at the latter's request without any remuneration being fixed from beforehand, the law always implies a reasonable

remuneration for the goods supplied or work done. This reasonable remuneration is known as *quantum meruit*. From the point of view of breach of contract, however, an action for *quantum meruit* arises in a different way. A contracts with B to build the latter's house for Rs. 30,000/- After A has proceeded with the work for sometime and before the building is completed B repudiates the contract and prevents A from proceeding with the work. In this case A can claim a *quantum meruit* for the work he has already done. He can further sue B for damages for breach of contract.

### (iii) Damage :

Where a party to a contract breches the contract, the injured party can sue the other party for such damages as will be just compensation for the loss he has actually sustained because of the breach. But he cannot expect to be compensated for all the losses he can trace to the breach of the contract. He is entitled to compensation for only such losses i.e. damages if (i) it is *reasonably* foreseen from the breach of contract, or (ii) were or might reasonably be supposed to have been in the contemplation of the parties at the time of entering into the contract. These two criteria for a proper estimate of loss suffered through breach of contract were laid down in the English case of *Hedley by Baxendale*<sup>1</sup>. The facts of the case are as follows. The owners of a flour mill sent a broken iron shaft to the office of the defendants who were common carriers to be conveyed by them to the carrier to whom it had been sent by the plaintiff mill owners. A pattern by which to make a new shaft. Due to the negligence of the carriers, i.e. the defendant, the delivery of the shaft was delayed and the plaintiff could not get a new shaft for many days as a result of which the plaintiff's mill was closed. Upon this the plaintiff sued the defendant for the loss of profits which would have been run if not the mill been closed. It was held that the carriers never contemplated at the time of the contract that the mill would be closed if the new shaft did not come quickly. The mill might easily have had a spare shaft under the same conditions. Of course, if the owners of the mill had informed the carriers at the time that the mill would be closed in case of delay in the delivery of the shaft, the case would have been different.

### Rule in Hadley vs. Baxendale :

Now let us consider each of the two criteria set down in the case of Hadley vs Baxendale

(1) Loss arising naturally out of the breach of contract  
Any number of consequences may flow out of the breach of contract  
some distant and some proximate. A man 'A' has his servant for a period of two years. Before the expiry of two years A dismisses B. The immediate consequence of the breach of contract is the loss to B of the wages. The remote consequence is may be any number B might, while looking for another job, catch influenza and incur expenditure on doctor's fee and medicine or be run over by a taxi and lose his leg. B can only recover the loss due to these remote consequences while it is not arise naturally out of the breach of contract.

(2) Loss which might reasonably be supposed to be in the contemplation of the parties at the time of the contract. Losses which might be remote may still be recovered by a plaintiff in an action for breach of contract provided such losses were contemplated by the parties at the time of the contract. We have seen before that the plaintiff in H. v. B. while could have recovered the cost of soft which might have incurred if he had engaged the delivery of the goods in view of that the mill could be used in his factory. But a xa

A party liable for breach of contract will not be entitled to recover for loss he must not suffer if he had not suffered the loss he will not be entitled to the moneyables which he might have received by one vicinage. A manufacturer cotton from B for the purpose of spinning his thread. B fails to supply the cotton. A should buy cotton elsewhere and sue B for the difference in price. He must not recover the loss by letting his mill close down and incurred other liabilities if he can get similar cotton elsewhere.

Damages for breach of contract is nothing but compensation for the loss suffered by the injured party. No extra damages are allowed even though the motive for the breach of contract was foul. Damages cannot be awarded to the injured party for injured feelings, mental worry and so incurred by the breach.

### **Penalty and Liquidated Damages :**

In many contracts the parties stipulate at the time of making the contract that a specified sum shall be payable for breach of it. The sum so fixed may be either—

- (i) Liquidated damages, i.e., a sum payable as damages the amount of which is determined by the parties beforehand, instead of being left to court, by a fair and honest estimate of probable losses likely to be caused by the breach.

*Or*

- (ii) A penalty, i.e., a sum which has no relation to probable losses which may arise and which has been stipulated by the parties *as in terrorem*, i.e., for the purpose of penalising a party who might break the contract.

If in the case of a breach of contract the court finds that a sum stipulated as damages in the contract is in the nature of liquidated damages, the court awards such a sum as damages without either increasing or reducing it. If, however, the court finds that the stipulated sum is in the nature of a penalty, the court *can* award such sum as damages, not exceeding the sum stipulated as the court thinks fit<sup>1</sup>.

Whether a stipulated sum is in the nature of liquidated damages or penalty is in every case determined by the court with reference to all the facts and circumstances of each case. A sum specifically mentioned as damages may still be found to be a penalty by the court if it thinks that the damages mentioned are excessive and unconscionable or bear no true relation to the loss which may result from breach. A contracts with B to pay Rs 100/- if he fails to pay B Rs 500/- on a given day. A fails to pay B 500/- on that day. B is entitled to recover from A such compensation, not exceeding Rs 100/- as the court considers reasonable. The reason is that the sum of Rs. 100/- bears no relation to the loss which B might suffer for the failure of A to pay Rs 500/- on the given day. Rs. 100/- is surely excessive and unconscionable.

### **Other Remedies for Breach of Contract :**

Apart from the remedies mentioned above there are two more remedies open to a party injured by a breach of contract, namely—

(1) *Specific Performance* : In certain cases of contracts damages do not give adequate relief to a party who suffers from a breach of contract. There the party breaking the contract is compelled by the court to perform his part of the contract by a decree of *specific performance*. B has a piece of antique. B contracts to sell the antique which A's father gave him. Afterwards he refuses to sell. Here the award of damages will not give A adequate relief. He does not want the money but the article. In such a case the court will issue a decree for specific performance to compel B to complete the sale. It is obvious that specific performance is granted only in rare cases.

(2) *Injunction* : An injunction is an order of the court restraining a party to a contract from breaking the contract. This is also granted in rare cases where damages fail to give adequate remedy. A theatre company engages an actor for three months. After the first month the actor signs a contract with some other theatre company. Here the proper remedy would be to restrain the actor from acting in the second theatre. In such a case the court will grant an injunction.

#### **Quasi Contracts or certain relations resembling those created by a Contract :**

There are certain transactions which give rise to obligations similar to those created by a contract though they are not contracts proper. These transactions are known as *quasi-contracts* and may be enumerated as follows :-

(1) If a person, incapable of contracting by law, e.g., an infant or a lunatic, or any one whom he is legally bound to support, i.e., his wife or children, is supplied by another person with necessaries suited to his condition in life, the person supplying such necessities is entitled to be reimbursed from the property of such person who is incapable of contracting.<sup>1</sup>

(2) A person who is interested in the payment of money which another is bound by law to pay, and who therefore pays it, is entitled to be reimbursed by the other. A holds his land as a tenant from his zemindar B. B fails to pay the government revenue for which A's tenancy is going to be annulled by revenue

<sup>1</sup> Section 68.

sale. A pays the revenue for B. He can claim the money back from B<sup>1</sup>.

(3) Where a person does anything for another person or delivers anything to him, not intending to do so gratuitously and such other person enjoys the benefit thereof, the latter is bound to make compensation to the former in respect of, or to restore, the thing so done or delivered. We have discussed this in connection with *quantum meruit*.<sup>2</sup>

(4) A person who finds goods belonging to another and takes them into his custody must restore them to the owner.<sup>3</sup>

(5) A person to whom money has been paid or anything delivered by mistake or under coercion must repay or return it.<sup>4</sup>

#### **Appropriation of payment :**

A debtor may be indebted to the creditor in respect of several sums, e.g., A borrows two sums of money, say Rs. 200/- and Rs. 400/- at different times. A in this case is indebted to B in respect of two sums. In such a case when the debtor pays money to the creditor he may either (i) specifically appropriate or apply to the payment to a particular debt or demand, or (ii) pay it generally in respect of his indebtedness.<sup>5</sup>

If the debtor wants to apply or appropriate the payment to a particular debt, he must intimate the creditor expressly or impliedly by conduct of his intention to do so *at the time of the payment*. The debtor cannot appropriate after he has made the payment already. The creditor is bound by the debtor's appropriation and cannot treat the payment as being made in respect of some other debt or towards indebtedness in general.

Where, however, the debtor has omitted to intimate and there are no other circumstances indicating to which debt the payment is to be applied, the creditor may apply it at his discretion to any lawful debt actually due and payable to him from the debtor, whether its recovery is or is not barred by the law of limitation.<sup>6</sup>

<sup>1</sup> Section 59.

<sup>2</sup> Section 70.

<sup>3</sup> Section 71.

<sup>4</sup> Section 72.

<sup>5</sup> Section 58.

<sup>6</sup> Section 73.

In *Mills v. Fowkes*<sup>1</sup> the facts were as follows. A was indebted to B for £100 - which was barred by the Statute of Limitation, and £150 which was not barred. A paid £15 without appropriating it to any particular debt. B sued A for £250 on the two debts. A pleaded as to the debt of £100 that it was barred and as to the debt of £150 a deduction of £15 - on account of the payment. It was held that as A did not appropriate the payment to the debt of £150, B could appropriate it generally on account and thus towards the barred debt of £100.<sup>2</sup> Thus B was held to be entitled to recover the £150.

### **Indemnity, Guarantee and Suretyship :**

A contract by which one party promises to cover or save the other from loss caused by the promisor or by a third person is called a *contract of indemnity*.<sup>3</sup> As ship is going on a long voyage. In consideration of a certain premium Indemnity and Lloyd's Insurance Co. undertakes to make good any loss which may be caused to A in case the ship or the cargo are lost on the sea. This is a pure case of a contract of indemnity.

A *contract of guarantee* on the other hand is a contract to perform the promise or discharge the liability of a third person in case of his default. A says to B, 'Lend C Rs 200/- and I shall pay you if C fails to repay.' This is an example of a contract of guarantee. Here A's liability to pay arises because he guarantees the payment of Rs 200 in case of C's default. But A's liability is, nevertheless, *secondary*. The primary liability is of C to pay and A's liability will arise only when C fails to pay back. The person who gives the guarantee is called the surety, the person in respect of whom a default the guarantee is given is called the *principal debtor* and the person to whom the guarantee is given is called the *creditor*. In the above case A is the surety, C is the principal debtor and B is the creditor.

There are two main differences between a contract of indemnity and a contract of guarantee:

<sup>1</sup> (1839) 5 Bing N S 455

<sup>2</sup> Section 124

<sup>3</sup> Section 126

(1) In a contract of indemnity the promisor undertakes a primary and not a secondary liability. Thus, Difference between Lloyds Co., in the above example, has the Indemnity and Guarantee. primary liability of covering the loss of A. But in a contract of guarantee the surety undertakes only a secondary liability.

(2) In a contract of indemnity there are only two parties, namely, the promisor and the party to be indemnified against loss. But in a contract of guarantee there must always be three parties, namely, the surety, who undertakes to discharge the liability of the principal debtor in case he defaults, the creditor, and the principal debtor.

The difference between the two types of contract is very well illustrated by *Guild vs. Conrad*<sup>1</sup>. There the defendant requested the plaintiff to accept the bills of exchange of a firm of Demerara merchants and promised that he would, if necessary meet the bills at maturity, i.e. if the firm of Demerara merchants failed to meet the bills, the defendant would meet them. Obviously, the liability of the defendant was secondary and is such the contract was a contract of guarantee. Subsequently, the firm of Demerara merchants fell into difficulties and the defendant asked the plaintiff to accept the bills of exchange drawn by the said firm and promised that he would supply funds in any event to meet the bills at maturity. In the latter contract the defendant apparently undertook the primary liability and the contract was, therefore, a contract of indemnity.

A guarantee which extends to a series of transactions which is to be performed by the principal debtor is called a continuing guarantee. A guarantees payment to B, a tea-dealer, to the amount £100/- for any tea he may from time to time supply to C. Here the guarantee relates to a series of supplies coming from B to C. B supplies C with tea to the value of £100/- and C pays B for it. Afterwards B supplies C with tea to the value of £200/- C fails to pay. The guarantee given by A was a continuing guarantee and he is accordingly liable to B to the extent of £100/-.

<sup>1</sup> (1894) 2 Q. B. 884 26 Digest 11 12

<sup>2</sup> Section 129.

A continuing guarantee may be terminated in the following two ways :-

(1) Revocation A continuing guarantee may be revoked at any time by the surety. After such revocation the surety is no longer liable for future transactions, but he still remains liable for all transactions completed before his notice of revocation reached the creditor A, in consideration of his discontinuing it. As request bills of (See 130-131) exchange for C guarantees to B, for twelve months, the due payment of all such bills to the extent of Rs. 500/- A revokes the guarantee after three months. But before the revocation B has discounted bills for C to the extent of Rs. 2000/- The revocation discharges A from all liability to B for any subsequent default. But A is liable to B for the 2000 rupees on behalf of C.

(2) Death of Surety The death of A puts to an end continuing guarantee as regards all future transactions unless there is an contract to the contrary.

The promisee in a contract of indemnity i.e. the indemnity holder has the following rights

(1) He can recover from the promisor all the loss which the Rights of an indemnity holder is subject to indemnity (See 125)

(2) He can recover all damage which he may be compelled to pay in substitution to the subject matter of the indemnity. New India Assurance Company insures A's car against all loss and accident. This is a contract of indemnity. A, driving his car negligently knocks over B's car and injures it. B sue A and the court awards damages against A. The New India Insurance Co. is liable to make good the damage to A.

(3) He can recover all costs necessary for bringing or defending such suit as mentioned in (2) above, provided he acted according to the orders of the promisor, or behaved as an ordinary prudent man would do under the circumstances, and did not act contrary to the promisor's instructions.

(4) He can also recover any money paid under a compromise in a suit as mentioned above.

The liability of the surety is co-extensive with that of the

principal debtor unless the contract provides otherwise. Until the debt or the liability of the principal debtor Liability of a surety (Sec. 128.) is discharged, the surety remains liable. Even the death of the principal debtor does not discharge the surety's liability. In case the principal debtor defaults, the creditor can proceed against the surety unless the contract provides that the creditor must proceed against the principal debtor first.

The following are the rights of the surety :

(1) The surety is entitled to proceed against the principal debtor in the same way as the creditor when the surety pays or performs all that he is liable for upon default of Rights of surety. (Sec. 140) the principal debtor. He is invested in this respect with all the rights of the creditor.

(2) If the principal debtor gives any security to the creditor at the time of the contract, the surety is entitled to the benefit of every such security. If the creditor loses or parts with the securities without the consent of the surety, the liability of the surety is reduced to the extent of the value of the securities. (Sec. 141).

The liability of the surety for the default of the principal Discharge of debtor is terminated or discharged in any one of surety. the following cases :

(1) By variation of the original contract. When the principal debtor and the creditor vary in any way the terms of their original contract by a subsequent agreement, the old contract is discharged, and along with it the liability of the surety, as to transactions subsequent to such variation, is also discharged, provided the variance was made by the creditor and the principal debtor without the consent of the surety. C agrees to appoint B as his clerk to sell goods at a yearly salary upon A's becoming surety to C for B's duly accounting for money received by him as such clerk. Afterwards C and B vary the terms of the employment contract without A's consent by stipulating that B should be paid a commission on the goods sold by him, instead of a yearly salary. If after this variation B fails to account for the goods he sold, A will not be liable to C, as C and B have made a variance in the terms of the original contract without A's consent (See 133).

(2) By the discharge or release of the principal debtor : If the liability of the principal debtor is discharged, the liability of the surety is also discharged. The liability of the principal debtor is discharged when either the creditor releases him by a fresh contract, or the creditor does something which amounts to a breach of contract and thus effects a discharge of the principal debtor. A gives a guarantee for B to C for the payment for goods to be supplied by C to B. C supplies goods to B and afterwards B gets into financial difficulties and contracts with C to transfer to him B's property in consideration of C releasing B from his liability to pay for the goods. Here B is released from his debt on account of the goods supplied by C, and A is also discharged from his liability as the surety. Now, let us illustrate how a breach of contract by the creditor discharges the principal debtor and along with him the surety. A contracts with B to grow crops of indigo on A's land and to deliver it to B at a fixed rate and C guarantees A's performance of the contract. B diverts a stream of water which is necessary for irrigation of A's land, and thereby prevents A from performing the contract. Here B's act amounts to an anticipatory breach of contract as he makes the performance of the contract by A impossible. A will, therefore, be discharged from all liability, and with him C will also be relieved of all liabilities as the surety<sup>1</sup>.

(3) By the creditor compounding, giving time, or agreeing not to sue the principal debtor : If the creditor comes to terms, or settles with the principal debtor, or if the creditor extends the time during which the principal debtor must pay or perform his contract, or if the creditor agrees with the principal debtor not to sue him, the surety is discharged and all his liability as the surety is terminated<sup>2</sup>. But the surety is not discharged when the contract to give time to the principal debtor is made by the creditor with a third person and not with the principal debtor<sup>3</sup>.

(4) By the creditor's act or omission impairing surety's eventual remedy : If the creditor does an act which interferes with the rights of the surety, or if the creditor does not do something which it is his duty to do, with the result that the

<sup>1</sup> S. 134.

<sup>2</sup> Section 135.

<sup>3</sup> Section 136.

surety is put to difficulty in enforcing his rights against the principal debtor, the surety is discharged. A puts M as apprentice to B and gives a guarantee to B for M's fidelity. B promises on his part that he will, at least once a month, see M make up the cash. B omits to see this done as promised and M embezzles the cash. A is not liable to B on his guarantee as B did not do what was his duty under the contract, namely, seeing M make up the cash at least once a month<sup>1</sup>.

#### **Agency :**

In the course of our study of the Law of Contract we have dealt with two parties entering into a contract.

**Definition of 'Agent' and 'Principal.'** In the vast business world of to-day it is not always possible for parties to come into direct contact for the purpose of entering into contracts.

I may have a cotton mill in the suburbs of Calcutta. To buy raw cotton I have to enter into contracts with cotton dealers in Bombay. To sell manufactured cloth I have to deal with retail merchants coming from all over Bengal. Is it possible for me to deal with these numerous people myself? Certainly not. Like all other businessmen I have to delegate my power to contract to people who will contract on my behalf. I may have my son in Bombay who contracts with cotton dealers there on my behalf. I may have another man at Dacca to contract with the local cloth-dealers there on my behalf and so on. All such people whom I may appoint to contract on my behalf are in the language of law my '*Agents*' and I am the '*Principal*' in relation to them. Sec. 182 of the Contract Act defines an *agent* as one employed to do any act for another or to represent another in dealings with third persons. The person for whom the agent acts or whom he represents is called the *principal*. The law of agency as laid down in the Indian Contract Act regulates the relationship between an '*agent*' and his '*principal*'. The foundation of the law of agency is the principle that what a person does by another he does himself—*Qui facit per alium facit per se*. A person can do by an agent all that a person wants to do or is compelled to do excepting those that can be performed only personally, as when a painter undertakes to paint a portrait himself.

### **Capacity to appoint or act as an Agent :**

Any person may act as an agent but an infant or a person of unsound mind cannot be appointed to act as an agent by a principal so as to be personally liable to the principal.<sup>1</sup> Any person who has capacity to contract can contract by an agent. But a person who is incapable of contracting by law cannot contract by an agent. Thus contracts made by an adult or other agent on behalf of an infant or a lunatic will not bind the infant or the lunatic unless they are contracts which would bind the estate of the infant or the lunatic if they were made by himself on his own behalf. Similarly a person who has a limited capacity to contract cannot make a contract by an agent which he cannot make personally. A company for instance can enter into only such contracts as are within the powers granted by its memorandum. If a Company makes a contract falling outside these powers by one of its agents such a contract will not bind the Company. The essence of agency proper is that the agent has no rights and duties under the contract. He merely a medium through whom the principal is connected contractually with third person. The agent's rights and duties are only in relation to his principal. Under the contract which he makes on behalf of his principal he has neither any right nor duty. But person who has no capacity, or only a limited capacity to contract e.g. a minor or a lunatic is competent to contract as a bind his principal to third parties. The reason is that the act of a agent is regarded as the act of the principal is between the principal and the 3rd parties. Thus a contract in writing entered into by an agent who did not understand the true purport of the contract could nevertheless bind the principal.<sup>2</sup>

### **Creation of Agency :**

As we have seen before no consideration is necessary to create an agency.<sup>3</sup> An agent without any remuneration is entitled to act on behalf of his principal as much as any other agent with remuneration and he has the same rights and duties as the latter. An agency can be created in any one of the following ways:

<sup>1</sup> Section 184

<sup>2</sup> See post, Part II

<sup>3</sup> Foreman v. Great Western Ry Co (1878) 38 LT 851 65198

<sup>4</sup> Section 185

- (1) By express or implied authority<sup>1</sup>.
- (2) By the principal giving his subsequent authority by ratification<sup>2</sup>.
- (3) By the principal being estopped from denying the authority of the agent<sup>3</sup>.

Let us now proceed to explain the above three ways.

(1) An agent can be appointed by express or implied authority. An authority is said to be express when it is given by words spoken or written. An authority is said to be implied when it is to be inferred from the circumstances of the case, things spoken or written and the usage or ordinary course of dealing are such circumstances from which authority is to be inferred. A has a studio where various customers come to have their photographs taken. A does not manage the studio himself. It is managed by B, who takes orders from customers, purchases chemicals and photographic goods from others and pays for them out of A's funds with A's knowledge. B has implied authority under such circumstances to enter into contract on behalf of A in respect of the business of the studio.

#### **Extent of Agent's Authority :**

An agent may be appointed to do one specific act or enter into one particular contract, in which case he is known as a *special agent*, or he may be entrusted with all acts of some general kind e.g., acts connected with a business in which case he is known as a *general agent*. But whether the agent is a special or a general agent, he is deemed in law to have authority to do every *lawful* thing which is necessary in order to do such particular acts or all acts of some general kind if he may be entrusted with. An agent having authority to carry on a business has authority to do everything which is either *necessary* or *usual* for the purpose of conducting such business. Obviously an agent conducting a business behalf of his principal is given greater authority by law as he can do not only things which are necessary but also those which are usual. Now, let us illustrate the above by the case of a special and a general agent.

<sup>1</sup> Sections 186, 187

<sup>2</sup> Section 196

<sup>3</sup> Section 237

<sup>4</sup> S. 188.

(a) A is employed by B residing in London to do one specific act, namely, to recover a debt due to B at Bombay. A may adopt any legal process, as a *special agent*, which is necessary to do the special act, namely, the recovery of the debt and may give a valid discharge for the same. But he cannot do anything which is usual but not necessary.

(b) A constitutes B his agent to carry on his business of Shipbuilder. B may do both *usual* and *necessary* things like the purchase of timber and other materials, hiring of workmen and so on, for the purpose of the business.

An agent has far wider authority in cases of emergency than in normal circumstances. In an emergency an agent can do all that a man of ordinary prudence would do in order to protect his principal from loss. A consigns provisions to B in an emergency at Calcutta with directions to send them (S. 189.) immediately to C at Cuttack. B may sell the provisions at Calcutta if it is found that the goods will be spoilt in course of their journey to Cuttack.

(2) We have seen above that an agent must have express or implied authority to contract on behalf of his principal. Otherwise the principal is not bound by the contracts he makes. But where the agent contracts on behalf of his principal without his previous authority, the principal may ratify such a contract. In case of such ratification, the principal is bound by the contract as if the agent had previous authority. Ratification may be done either by words spoken or written or by implied conduct. The following example will illustrate ratification by implied conduct. A, without B's authority, lends B's money to C. Afterwards B accepts interest on the money from C. B's conduct implies a ratification of the loan.

No valid ratification can be made by a person whose knowledge of the facts of the case is materially defective. If the principal can show that he did not possess full knowledge of all the facts when he ratified, he will not be bound by the ratification<sup>1</sup>.

No person can ratify the acts of another which were done on his behalf, but without his authority, and the effect of which is to deprive some third person of his property rights or to subject

<sup>1</sup> Section 198.

such third person to damages<sup>1</sup>. A holds a lease from B terminable on three months notice. C, an unauthorised person, gives notice of termination to A. The notice cannot be ratified by B, so as to be binding on A.

(3) The principle of estoppel is laid down in s. 115 of the Indian Evidence Act<sup>2</sup>.

Applied to agency it is that a person who holds out some other person as his agent, though in fact he is not his agent, is bound by contracts entered into by the latter with third persons.

<sup>Agency by</sup> <sup>Estoppel</sup> S. 23, persons. The principle behind this rule is that a person, who holds out another before the general public either by his words or conduct, as the person or agent entrusted to do a particular act or general business on his behalf, will be estopped from denying liability arising out of contracts entered into by such agent. Thus, in *Soules v. L. S. W. R.* the plaintiff entrusted his luggage with a porter wearing the uniform of the defendant Railway Co. The luggage was stolen. The Railway Co. wanted to avoid liability for the loss on the ground that the porter was off duty. But it was held that the porter who held out by the Company is in agent authorised to receive luggage and is such the Company was bound by his acts.

Agency by estoppel arises in three ways:

- (1) A person may hold out another as his agent although that other is not or has never been his agent.
- (2) A person may hold out his agent as having a wider authority than he was given authority for. In *Wittman v. Fenwick*,<sup>3</sup> the manager of a public house had only the authority to buy mineral water and bottled beers but the manager bought some cigars though he had no authority to do so. The owners of the public house were held liable for the cigars as they by their conduct, held out the manager to conduct everything connected with the public house.
- (3) A person may hold out another as his agent although that other has ceased to be so. In *Frumian v. Loder*,<sup>4</sup>

<sup>1</sup> Section 200.

<sup>2</sup> See infra, Part I.

<sup>3</sup> (1919), 88 L.T. K.B. 524.

<sup>4</sup> (1892) 1 Q.B. 346.

<sup>5</sup> (1840) 11 A. & E. 589.

Loder's agent H used to sell tallow in the form "Sold for L." After some time H ceased to be L's agent. But L did not notify that to his customers. So when H contracted to sell tallow to the plaintiff, Loder was held liable for the contract.

### **Agent's duty to Principal<sup>1</sup>:**

An agent has the following duties towards his principal:

(a) An agent is bound to conduct the business of his principal according to the directions given by his principal. If there are no directions given by the principal, he must follow the custom or usage prevailing in the trade. If he acts contrary to such directions or custom he must make good any loss sustained thereby and if there is any profit he must also account for it. The following illustrations will make the principle clear:

- (i) A, an agent, carries on a business on behalf of his principal B. There is a custom in the business to invest funds until all moneys left in hand. A does not invest such moneys. A must make good to B the interest which B usually derives from such investments.
- (ii) B, a broker, carries on business on behalf of A. It is not the custom of the trade to sell on credit. B sells A's goods to C on credit. C becomes insolvent and fails to pay. B will be liable to make good the loss to A even if C's credit was very high at the time, as he acted contrary to the custom. It would have been the same if instead of being a custom it was A's direction not to sell on credit.

(b) An agent must discharge his duties with ordinary skill and reasonable diligence. By ordinary skill is meant skill possessed by person in similar position, and by reasonable diligence is meant not perfect or utmost diligence but such diligence as can be expected from men of ordinary prudence. Of course in every case the court decides whether ordinary skill or reasonable diligence has been exercised or not according to the circumstances of the case. If the principal suffers loss through want of

<sup>1</sup> Sections 211, 221.

the agent's ordinary skill or reasonable diligence, the agent must make good the loss. But the agent is not, however, liable for all the losses which might be traced to his want of skill or diligence. Here, as in the case of damages for breach of contract, the rule in *Hadley v. Baxendale* is followed. The agent is liable only for losses which arise directly out of his want of ordinary skill or reasonable diligence and he is not liable for remote losses. The following illustration will make it clear.

A has an agent B in London. A sum of money is paid to B on A's account, with orders to remit. B retains the money, for a considerable time. A, in consequence of not receiving the money, becomes insolvent. B is liable for the money and interest at the usual rate from the day on which it ought to have been paid and for any further loss due to factors like a variation in the rate of exchange but not for any other remote consequences.

If, however, a principal appoints an agent with full knowledge of his want of skill and diligence, the principal cannot recover any loss which might be caused by the agent's neglect.

(c) An agent is bound to render proper accounts to his principal on demand.

(d) An agent must use all reasonable diligence to obtain instructions from his principal in cases of difficulty. If he can obtain such instructions but fails to do so and thereby brings loss to his principal, he must make good such loss.

(e) If an agent deals in the business of the agency or his own account either by dishonestly concealing material facts from his principal or by carrying on transactions to the disadvantage of his principal, the principal can repudiate the transactions. A directs B his agent to sell his house. B buys the house himself in C's name. A can repudiate the sale if he can show that B has dishonestly concealed any material fact or that the sale has been disadvantageous to him.

(f) If an agent deals in the business of the agency on his own account instead of on account of his principal, without the knowledge of his principal, the principal is entitled to claim any benefit which the agent has gained. A directs B his agent to buy a certain house for him. B buys the house himself and tells A that the house cannot be bought. A may, on discovering that B has bought the house, compel him to sell to A at the price he gave for it.

### **Principal's duty to agent.<sup>1</sup>**

A principal has the following duties towards his agent --

(a) A principal is bound to compensate or indemnify his agent against the consequences of all *lawful* acts done by such agent in the exercise of the authority conferred upon him. B at Singapore, under instructions from A at Calcutta, contracts with C to deliver certain goods to him. A does not send the goods and C sues B for breach of contract. A asks B to defend the suit. B is ordered to pay damages and costs and incurs expenses. A is liable to B for such damages, costs and expenses.

(b) A principal is bound to indemnify the agent against the consequences of any act which the agent does in good faith at the instance of the principal, though the act causes injury to the rights of third persons. B at the request of A sells goods in the possession of A and hands over the proceeds to A. A had no right to dispose of the goods. But B did not know that C, the true owner of the goods, sues B and recovers the value of the goods and costs. A is liable to indemnify B for what he has been compelled to pay to C and for B's own expenses.

(c) A principal is not bound to indemnify his agent for the consequences of any criminal act which the agent does at the request of the principal. The reason is that no one can protect himself from criminal liability by pleading that he was merely an agent. A employs B to beat C and agrees to indemnify him against all consequence of the act. B thereupon beats C and has to pay damages to C. A is not liable to indemnify B for those damages.

(d) A principal must make compensation to his agent for any injury caused to him through the principal's neglect. A employs B as a bricklayer in building a house and puts up the scaffolding himself. The scaffolding is unskillfully put up and B is in consequence hurt. A must make compensation to B.

(e) A principal must pay the remuneration, commission or other dues to the agent. In the absence of any contract to the contrary, an agent cannot claim any payment until the completion of the act for which he is constituted an agent. But an agent may return money received by him on account of goods sold il-

<sup>1</sup> Sections 222-225

though the whole of the goods consigned to him for sale may not have been sold. In the absence of any contract to the contrary, an agent is also entitled to retain goods, papers and other property, whether movable or immovable, of the principal received by him until the amount due to himself for commission, disbursements and services in respect of the same has been paid or accounted for to him.

#### Effect of agency on contract with third persons.<sup>1</sup>

When a person contracts by his agent or acts through his agent his rights and liabilities are just what they would have been had he contracted or acted himself. A buys goods from B knowing that B is an agent for their sale but not knowing who is the principal. B's principal is the person entitled to claim from A the price of the goods, and similarly A can sue the principal, when he discovers him, for any breach of contract.

#### Liability of principal when agent exceeds authority.<sup>2</sup>

We have seen before that an agent must have authority, implied or express, to act on behalf of his principal, unless, of course, the principal ratifies the act of the agent subsequently. Where the agent exceeds the authority given by the principal, the principal is not bound by contracts lying outside the powers granted to the agent. A authorises B to buy 500 sheep for him. B buys 500 sheep and 200 lambs for one sum of 6000 rupees. A may repudiate the whole transaction, for B has exceeded his authority by buying 200 lambs. But in some cases where an agent exceeds his authority, some acts he does fall within such authority and some acts fall outside it. When the part of what he does which is within his authority can be separated from the part which is beyond his authority, the principal will be bound by such acts as fall within his authority. In the above illustration let us suppose that A buys 500 sheep and 200 lambs in separate lots and pays for them in two separate lumps of Rs. 400/- and Rs. 2000/- instead of in one lump of Rs. 6000/-. Here obviously the purchase of 500 sheep falls within the authority of B and it can be separated from the purchase of 200 lambs which falls outside such authority. A will, therefore, be bound by the purchase of 500 sheep by B.

<sup>1</sup> Sections 226, 238.  
<sup>2</sup> 227, 228.

### **Notice given to an agent.**

Notice of any fact given to an agent is deemed to be notice given to the principal provided such agent has got authority to receive such notice, or in the usual course of business or by custom such agent receives such notice. An agent receiving such notice must also receive it in course of his duty as an agent in order that the notice may operate as a notice to his principal. A draws a hundi on his Bombay office in favour of the firm of B & Co. B & Co. informs the cashier of A's office in Bombay that the hundi has been stolen. The cashier does not inform the office and when he is away on leave the stolen hundi is presented and cashed. A is bound to pay to B & Co. over again, as the notice of the theft communicated to his cashier is notice to himself, since the cashier is deemed capable of receiving such notice. But if in the above case the durwan of A's office was told of the theft, A would not have been bound by the notice for the durwan is neither authorised nor is it usual in the normal course of business for him to receive such notice. Also if the cashier knew of the theft from some one not connected with B & Co. or in course of his private dealings unconnected with his duty as a cashier A would not have been bound by such notice.

### **Agent's right and liability under the contract he makes.<sup>1</sup>**

In the absence of any contract to the contrary an agent can not personally enforce contracts entered into by him on behalf of his principal nor is he personally bound by them. A has an agent B. B contracts with C for the sale of A's house. If C refuses to buy the house later on, it is A who can sue C for breach of contract. Similarly if A refuses to sell the house it is A whom C must sue. But any contract can of course make provision for the personal liability of the agent and in such a case the agent can enforce the contract himself and will himself be liable under the contract. In the following cases of contract the personal liability of the agent is presumed<sup>2</sup>.

(1) Where the contract is made by an agent for the sale or purchase of goods for a merchant resident abroad. A is the agent in Calcutta of B who is a merchant in London. A can enforce all

<sup>1</sup> Section 230

contracts he makes in Calcutta on behalf of B, and will be liable under them to persons with whom he contracts.

(2) Where the principal, though disclosed, cannot be sued. Foreign ambassadors, or heads of states, or sovereigns cannot be sued. Their agents entering into contracts with others are therefore personally liable on contracts they make.

(3) Where the agent acts as an agent but does not disclose the name of his principal. A enters into a contract with B knowing that he is an agent but ignorant of the name of the principal. B is liable to A personally under the contract and he can also enforce the contract against A. B would have been equally liable if A did not know or had no reason to suspect that he was an agent at all.

### **Undisclosed Principal :**

(1) If an agent makes a contract with a person who neither knows nor has reason to suspect that he is an agent the principal of the agent is known as undisclosed principal. He can disclose himself and ask for the performance of the contract. The other contracting party will also have against the principal all the rights he would have had against the agent if the agent had contracted for himself. B contracts to buy some cotton from C, a cotton dealer. B is really contracting for A his principal, but C does not know, nor has he any reason to suspect that B is A's agent. In this case B can obviously sue C if he refuses to sell the cotton, and C can also sue B if he refuses to buy the cotton. A can also sue C or be sued by C. As a principal he can always require the performance of the contract by the other party and the other party can similarly make him liable under the contract.

If a principal is totally undisclosed like A in the above case the other contracting party C in the above case can refuse to fulfil the contract if the principal if he disclosed himself, provided he can show that he would not have entered into the contract if he had known who was the principal, or if he had known that the agent is not the principal.

We have just seen that in undisclosed principal can always require the performance of a contract entered into by his agent with another person who neither knew nor had any reason to

suspect that the agent was an agent but the principal is entitled to obtain such performance subject to the rights and obligations subsisting between the agent and the other party to the contract A, who owes 500 rupees to B, sells 1000 rupees worth of rice to B. A is acting as agent for C in the transaction, but B has no knowledge nor reasonable grounds of suspicion that such is the case. C cannot compel B to take the rice without allowing him to deduct from the price A's debt of Rs 500/-

### **Right of person dealing with agent personally liable.**

In cases where the agent is personally liable, a person dealing with him may hold either him or his principal or both of them liable<sup>1</sup>

### **Liability of a pretended agent :**

If a person falsely represents himself to be the agent of another and thereby induces a third person to enter into a contract with him as agent, such a pretended agent is liable to make good any loss which such other person incurs as a result of entering into the contract. The pretended agent will, however, be exonerated from the liability if his alleged principal ratifies the contract subsequently

### **Effect of fraud or misrepresentation by Agent :**

If an agent makes a misrepresentation or commits a fraud, agreements entered into by others on the basis of such fraud or misrepresentation will be voidable at the option of the injured party as if the principal had made the misrepresentation or committed the fraud. But if the agent makes a representation or commits a fraud in matters not falling within his authority the principal cannot be made liable thereby

### **Termination of Agency :**

An agency is terminated i.e. in event cause to be an agent, in the following ways<sup>4</sup>

- (1) Revocation, express or implied by the Principal, or renunciation by the Agent

<sup>1</sup> Section 233

<sup>2</sup> Section 236

<sup>3</sup> S. 255

<sup>4</sup> Section 201

- (2) By the business of the agency being completed or by the expiration of the time for which the agent was appointed.
- (3) By the death or insanity of either the principal or the agent.
- (4) By the principal being adjudged an insolvent.

These points require a little explanation :--

(1) **Revocation and Renunciation** :--The principal can terminate an agency by revoking *i.e.* by withdrawing the authority given to the agent. ¶ But where an agent has himself an interest in the property which forms the subject matter of the agency, the principal cannot terminate the agency by revocation unless there was a contract before providing for such revocation. A gives authority to B to sell A's land so that B can take out of the proceeds the debts due to him from A. A cannot revoke this authority, nor can it be terminated by his death or insanity, as B has an interest in the property as a creditor. Subject to this qualification a principal may revoke the authority given to his agent *at any time before the agent has exercised the authority in as to bind the principal*<sup>1</sup>. ¶ The principal *cannot* revoke the authority given to his agent after the authority has been partly exercised by the agent in such a way that he has incurred personal liability and the revocation will expose him to loss or injury<sup>2</sup>. A authorises B to buy 1,000 bales of cotton on account of A and to pay for it out of A's money remaining in B's hands. It buys 1000 bales of cotton in his own name so as to make him personally liable for the price. A cannot revoke B's authority so far as regards payment for the cotton. If, however, in the above case B buys the cotton in A's name so as not to make himself personally liable, A can revoke B's authority to pay for the cotton.

The agent can also terminate the agency by renunciation, *i.e.* by giving notice to the principal of his unwillingness to act as agent.

Where the agency is fixed by contract to continue for a specified period, either the principal or the agent can previously terminate the agency by revocation in one case and renunciation in the other for a just cause. But if there is no just cause, the

<sup>1</sup> Section 203.

<sup>2</sup> Section 204.

principal must make compensation to the agent if he revokes, and the agent must make compensation to the principal if he renounces before the specified period<sup>1</sup>.

Whether the principal revokes or the agent renounces reasonable notice must be given by the one to the other otherwise the damage thereby resulting to the principal or the agent, as the case may be, must be made good to the one by the other.

Revocation and renunciation may be either expressed in words or writing, or may be implied in the conduct of the principal or the agent respectively. A empowers B to let A's house. Afterwards A lets it himself. This is an implied revocation of P's authority.

Where an agent's authority is revoked, the revocation does not affect the rights and liabilities of the agent in relation to the principal until the agent is actually informed of the revocation, and the revocation does not affect the rights and liabilities of the general public with whom the agent deals in relation to the principal, unless the notice of revocation reaches the public. A directs B to sell goods for him on a commission of 5% on the net proceeds. Letter from A revokes B's authority by a letter. But before the letter reaches B, B sells the goods for Rs. 100/- The sale is binding on A and B is entitled to his commission. Let us assume that on the above instance C, a member of the public, knows that A has directed B to sell A's goods. But C does not know of A's letter by which A revoked B's authority. He buys the goods from B for Rs. 100/- in full with the money. As C is not informed of A's letter of revocation, his payment to B is good and he can keep the goods.

(2) If A employs B to sell his house or to manage his business for six months, B's agency will terminate after B has sold the house or managed the business for six months.

(3) The relation between an agent and the principal is entirely personal. Therefore the death or incapacity like its insanity of either terminates the agency.

(4) A person who has been adjudged an insolvent cannot act as a principal. Therefore, as soon as a person is adjudged an

<sup>1</sup>Section 205

<sup>2</sup>Section 207<sub>m</sub>

insolvent, all persons who were before or at the time of his insolvency his agents, cease to be so after his adjudication as an insolvent.

### **Sub-Agent :**

The general rule of law is that an agent cannot appoint another person to do his duties which he owes to his principal —*deligatus non potest delegare*—a delegate cannot delegate. But in some cases an agent can appoint a sub-agent to do his duties where it is usual according to the usual mode of business and custom. A, a cotton dealer in Bombay, has an agent B in Calcutta to sell cotton for him. There are many duties, like those undertaken by banks, which agents like B generally delegate to banking concerns. Or it may be that B has to appoint solicitors to do all the legal work for him in his business as an agent. The banks and the solicitors in this case are sub-agents.

A sub-agent has been defined in the Contract Act as a person who is a sub-agent employed by and acting under the control of the original agent in the business of the agency.

Sec. 191. Where a sub-agent has been properly appointed, i.e. where such appointment is usual, the sub-agent is only responsible to the agent and not to the principal. The agent, however, is responsible to the principal for the sub-agent. If the sub-agent is guilty of wilful wrong or fraud, the principal can directly hold him responsible.

Where an agent has express or implied authority to appoint a sub-agent and a sub-agent has been properly appointed, the principal is liable for all the acts of the sub-agent. Liability to the in relation to third parties. But where an agent public for the act improperly appoints a sub-agent, i.e., where he has no express or implied authority, or where it is not usual to appoint a sub-agent, the agent is liable for all the acts of the sub-agent both to the principal and third parties. The principal is not bound by or responsible for the acts of the person so employed, nor is that person responsible to the principal.

It should be carefully noted here that an agent can not only appoint a sub-agent where it is usual, he can also have authority,

express or implied, to nominate or select another person to act as agent for the principal. Where a person has been so nominated by an agent, he becomes *not a sub-agent, but an agent* of the principal, and he is related to the principal in the same way as the agent nominating or selecting him. In selecting such an agent for the principal, an agent must use such ordinary prudence as he would have done had he been the principal himself. If he does thus he is not responsible to the principal for the acts or negligence of the agent so selected<sup>1</sup>

'Bailment' is a technical term of English Common Law, though literally it may mean any kind of handing over. The Indian Contract Act<sup>2</sup> defines a bailment as the delivery of goods by one person to another for some purpose, upon a contract that they shall, when the purpose is accomplished, be returned or otherwise disposed of according to the directions of the person delivering them. The person delivering the goods is called the 'baileor.' The person to whom they are delivered is called the 'bailee.' A goes to Fipos for his lunch and leaves his hat with the cloak room attendant during the time he is having his lunch. Here A is the baileor, Fipos are the bailee, and the purpose for which the hat was bailed was that it might be kept when A has his lunch, and the hat has to be returned to A when he finishes his lunch and goes out.

If a person already in possession of the goods of another contracts to hold them as a bailee, he thereby becomes the bailee, and the owner becomes the baileor, of such goods although they may not have been delivered by way of bailment. Let us assume that in the above instance A goes to a hat shop and buys a hat already in the shop. He then leaves the hat in the shop for the shop owners to send it to his house. Here though A did not actually hand over the hat to the shop owners, yet the shop owners will be the bailees and A the baileor, because of the implied contract made by the shop owners to act as such. In this case A is deemed to have delivered the hat to the shop-owners *constructively by way of bailment*.

<sup>1</sup> Sections 194, 195.

<sup>2</sup> Section 148.

### **Delivery to bailee :**

To constitute a contract of bailment delivery must be made to the bailee. This delivery may be either actual or constructive. Actual delivery means physically handing over the goods bailed to the bailee or someone so authorised to hold on his behalf, as when A, in our previous illustration, actually gives his hat to the cloak room attendant who is authorised to take the hat on behalf of Firpos. Constructive delivery means transferring possession without actually handing over the goods physically, as, when A, in the above illustration, leaves the hat in the shop. The most important thing about delivery is that the bailor must transfer his possession to the bailee. Thus, I can deliver my motor car to a garage as my bailee by simply giving the garage my key or delivery order to the warehouse, where my car is stocked.

### **Different kinds of bailment.**

Bailment may be of different kinds and they may be classified as follows:

- (1) Bailment for safe custody or Bailment for use.
- (2) Bailment for reward or gratuitous bailment.

1 A bailment of the first kind arises when the bailor delivers an article to the bailee for simply keeping it in safe custody. A gives his camera to B for the latter to keep it in his custody for six months. This is a case of bailment for safe custody.

When, however, the bailor delivers an article to the bailee for the latter to use it in any specific or general way, it constitutes a bailment for use. Let us assume that in the above illustration A gives his camera to B for six months for the latter to use it in taking portraits. Here the bailment is a bailment for use.

2 Whether the bailment is for use or for safe custody, the bailee can either charge for his services or render them free. When the bailee charges for his services the bailment is a bailment for reward. When however the bailee does not charge anything, the bailment is gratuitous.

### **Duties or responsibilities of the bailor :**

The bailor bears certain duties and responsibilities towards the bailee which may be enumerated as follows:

- (1) The bailor must disclose to the bailee faults in the goods bailed, of which the bailor is aware and which materially interfere

with the use of them, or expose the bailee to extraordinary risks, and, if he does not make such disclosure he is responsible for damage arising to the bailee directly from such faults.

If, however, the goods are bailed for hire, the bailor is responsible for such damage not only where he was aware of the existence of such faults but also where he was *not aware* of the existence of such faults in the goods bailed.<sup>1</sup>

These two principles will be clear from the following examples -

(a) A keeps with B certain boxes which A knew contained highly inflammable chemicals. A does not disclose to B that the boxes contain inflammable material. Later on one of the boxes catches fire and B's store house is gutted. A must make good the loss B sustains.

(b) A hires a cart of B. The cart is unuseful though B is not aware of it and A is injured. B is responsible to A for the injury, although he was not aware of the defect in the cart as the cart was hauled out *on hire*.

(2) The bailor must repay to the bailee all the expenses which the bailee has to incur when the conditions of the bailment are such that the goods are to be kept or work has to be done upon them by the bailee for the bailor and the bailee will not receive any remuneration. A keeps his horse in B's stable and B agrees to this without any remuneration. But the horse has to be fed and looked after and A must repay to B all that the latter has to spend for keeping the horse even though B charges no remuneration for himself. Take for instance the case of bailment which involves the carrying of goods. B agrees to take and drive A's car to A's brother free of charge but B has to buy petrol in order to drive the car to A's brother's place. A must repay to B the sum B has to spend on petrol.

(3) The bailor is responsible to the bailee for any loss which the bailee may sustain due to the following reasons<sup>2</sup> -

<sup>1</sup> Section 150

<sup>2</sup> Section 158

<sup>3</sup> Section 164

- (a) The bailor was not entitled to make bailment A gives a car, which belongs to B, to C, an auctioneer, for the latter to put it on auction C, believing that the car really belongs to A, sells the car on auction to a third person B sues C for damages for the unauthorised sale A must compensate C for any damages that the court may award against C
- (b) The bailor was not entitled to receive back the goods
- (c) The bailor was not entitled to give directions respecting the goods bailed

#### Duties of the Bailee :

The bailee has certain duties towards the bailor These may be set out as follows —

(1) In all cases of bailment the bailee is bound to take as much care of the goods bailed to him as a man of ordinary prudence would, under similar circumstances, take of his own goods of the same bulk, quality and value as the goods bailed<sup>1</sup> If the bailee takes as much care as a man of ordinary prudence, he is not responsible for the loss, decay, action or deterioration of the thing bailed But if he fails to take such care, he will be held responsible for all damages caused through want of such care What is ordinary prudence is in every case determined by the court with reference to all the circumstances of the case, the usage and custom relating to the bailment of the goods in question and so on Suppose A bails his goods to B for safe custody and B keeps them in this warehouse Due to a chunk in the roof of the warehouse, water trickles through and spoils the goods B is responsible for the loss to A as the loss would not have been caused if B had used ordinary prudence in having the roof repaired If however, instead of water trickling through the chunk, the goods were destroyed due to the warehouse being damaged by a cyclone B would not have been responsible for the loss as B could not have prevented the cyclone by using ordinary prudence

(2) If the bailee, with the consent of the bailor, mixes the goods of the bailor with his own goods, the bailor and the bailee shall have an interest in proportion to their respective shares in

<sup>1</sup> Section 151

<sup>2</sup> Section 152

the mixture thus produced. A bails 20 seers of flour to B. B with A's consent mixes 10 seers of his own flour with A's. In the total mixture A's share will be  $\frac{2}{3}$  and B's  $\frac{1}{3}$ <sup>1</sup>.

(3) If the bailee, without the consent of the bailor, mixes the goods of the bailor with his own goods and the goods can be separated or divided, the property in the goods remains in the parties respectively; but the bailee is bound to bear the expense of separation or division, and any damage arising from the mixture. C bails 100 bales of cotton marked with a particular mark to B. B, without C's consent, mixes the 100 bales with other bales of his own, bearing a different mark. C is entitled to have his 100 bales returned, and B is bound to bear all the expenses incurred in the separation of the bales and any other incidental damage<sup>2</sup>.

(4) If the bailee, without the consent of the bailor, mixes the goods of the bailor with his own goods in such a manner that it is impossible to separate the goods bailed from the other goods and deliver them back, the bailor is entitled to be compensated by the bailee for the loss of the goods. A bails a barrel of cape flour worth Rs. 45/- to B. B, without A's consent, mixes the flour with country flour of his own, worth only 25 - a barrel. B must compensate A for the loss of his flour<sup>3</sup>.

(5) The bailee must return or deliver according to the bailor's directions, the goods bailed, without demand, as soon as the time for which they were bailed has expired, or the purpose for which they were bailed has been accomplished<sup>4</sup>.

(6) The bailee is bound to return, deliver or tender the goods bailed at the proper time. If he fails to do that, he is responsible to the bailor for any loss, destruction or deterioration of the goods from that time<sup>5</sup>.

(7) The bailee is bound to deliver to the bailor or anyone whom the bailor directs, any increase of profit which may have accrued from the goods bailed. A leaves a cow in the custody of B to be taken care of. The cow gives birth to a calf. B is bound to deliver the cow as well as the calf to A<sup>6</sup>.

<sup>1</sup>Section 155.

<sup>2</sup>Section 156.

<sup>3</sup>Section 157.

<sup>4</sup>Section 168.

<sup>5</sup>Section 161.

<sup>6</sup>Section 163.

(8) The bailee must compensate for the loss of the bailor if the loss is caused due to some act not authorised by the contract of bailment. A lends a horse to B for his own riding only. B allows C, a member of his family, to ride the horse. C rides with care but the horse accidentally falls and is injured. B is liable to make compensation to A for the injury done to the horse. If the bailee does some act which is not only unauthorised but also inconsistent with the contract of bailment, the bailor, in addition to his remedy of compensation, can also treat the contract as void at his option. A lets to B, for hire, a horse for his own riding. B drives the horse in his carriage. Using the horse to draw a carriage is inconsistent with the agreement to use the horse for riding. If the horse is injured A is entitled to compensation. But A has another remedy. Whether the horse is injured or not, A can treat the contract as void, i.e., he can bring back the horse even though the time for which the horse was let out has not expired<sup>1</sup>.

### **Termination of Bailment :**

A bailment contract comes to an end in the following ways :-

(1) When the time for which the goods were bailed has expired, or the purpose for which the goods were bailed has been accomplished, the contract of bailment comes to an end. A lends B his tractor plough for twelve months. The bailment will terminate on the expiry of twelve months. A lends B his tractor plough for B to plough his piece of land. The bailment will terminate as soon as B has finished ploughing his land.

(2) A gratuitous bailment is terminated by the death either of the bailor or of the bailee.

(3) When a bailee does an act inconsistent with the contract of bailment, the bailor can terminate the bailment at his option (See *ante* "duties of the bailee").

### **Bailee's Particular Liens :**

When a bailee has rendered services, in pursuance to the bailment contract, involving exercise of labour and skill, the bailee has, unless he has contracted to render such services free, a right

<sup>1</sup> Sections 153 and 154.

to retain the goods bailed until he receives due remuneration for services he has rendered<sup>1</sup>

A delivers a rough diamond to B, a jeweller, to be cut and polished, which is accordingly done. B is entitled to retain the stone until he is paid for his services.

We have seen above that a bailee can retain the goods until he is paid for the services he has rendered in connection with the goods. The bailee cannot, however as a general rule, retain the goods for unpaid amounts due from the bailor in regard to other accounts or in regard to services rendered in connection with other goods. Therefore, generally a bailee's lien is *particular*. But bankers, solicitors, factors, wharfingers<sup>2</sup> and policy-brokers have a *general* lien. They can retain goods or securities of their customers on account of debts which are not in any way connected with the goods or securities in question. A deposits a few shares to get an advance of Rs. 1000/- from a bank. A repays the advance later on. But it is found that A had previously taken an advance of Rs. 500/- without any security. The bank may retain the shares until A repays the previous advance of Rs. 500/-. In the same way, a solicitor can retain all the papers and documents of his client in his hands until he is paid his fees. Thus, this class of persons can retain the goods not only against a *particular account* but also against a *general balance of account*. Excepting the bailees mentioned above no other bailees enjoy a general lien. Goods retained on general lien cannot be sold for the realisation of dues. They can only be retained. Goods retained on particular lien can be sold if there is an agreement to that effect<sup>3</sup>.

#### Bailment of Pledges :

The bailment of goods as security for payment of a debt or performance of a promise is called 'pledge'. The bailor in this case is called the 'pawner' and the bailee is called the 'pawnee'<sup>4</sup>

**Rights of the pawnee.** The rights of the pawnee may be stated as follows :—

<sup>1</sup> Section 170.

<sup>2</sup> Owner of wooden or stone platform beside which ships are moored for loading or unloading cargo.

<sup>3</sup> Section 171.

<sup>4</sup> Section 172.

- (a) The pawnee may retain the goods pledged not only for payment of the debt or performance of the promise, but for interest on the debt, and all necessary expenses incurred by him in respect of the possession or for the preservation of the goods pledged. But the pawnee cannot, unless there is a contract to the contrary, retain the goods pledged for any debt or promise other than the debt or promise for which they are pledged<sup>1</sup>
- (b) The pawnee is entitled to receive from the pawnor extraordinary expenses incurred by him for the preservation of the goods pledged
- (c) If the pawnor makes default in payment of the debt or performance at the stipulated time of the promise, the pawnee may bring a suit against the pawnor upon the debt or promise and retain the goods pledged as security or he may sell the goods by giving the pawnor reasonable notice. If the proceeds of such sale are less than the amount due in respect of the debt or promise, the pawnor is still liable to pay the balance. If the proceeds of sale are greater than the amount of due the pawnee shall pay over the surplus to the pawnor.

Where the pawnor fails to pay his debt or perform his promise

**Rights of the pawnor**      if the stipulated time, he has the right to pay his debt or perform his promise at any time before the sale of the goods pledged and redeem the goods.

<sup>1</sup> Sections 173 and 174

## CHAPTER II

### SALE OF GOODS

*(Indian Sale of Goods Act)*

#### **History :**

The Indian law regarding the sale of goods was, until the passing of the Indian Sale of Goods Act, 1930, contained in Chapter VII of the Indian Contract Act of 1872. In 1926-27 an exhaustive examination of the case law bearing on certain portions of the Indian Contract Act, 1872, including Chapter VII, which embodies law relating to the sale of goods, was made in the Legislative Department under the supervision of the late Mr S R Das, the then Law Member of the Executive Council of the Governor General. In 1928 the results of that examination were considered by the late Sir Din Shaw Mulla, at that time holding the office of the Law Member. A draft bill was prepared on the lines of the English Sale of Goods Act, 1893, embodying the provisions of law relating to the sale of goods in a separate enactment. The draft bill after going through a select committee was ultimately passed and became the Indian Sale of Goods Act, 1930. Before the passing of the Indian Contract Act, 1872, Chapter VII of which contained the law relating to the sale of goods in movables, the law on this subject was not only not uniform throughout British India, but was also outside the limits of the Original Jurisdiction of the High Court, extremely uncertain in its application. Within the limits of the Presidency towns the rules of English law including those in Statute of Frauds, were applied, whilst in the mofussil, it was doubtful whether the Statute of Frauds was applicable. To remedy this unsatisfactory state of affairs, Chapter VII of the Indian Contract Act was framed and except in regard to the rule as to market overt, the law embodied in Chapter VII represented generally the English law on the subject as it then stood.

A contract for sale of goods is not a separate kind of contract. It is only a species of the wider kingdom of contracts and it is governed by all the rules of law which pertain to contracts in general. The reason why a separate law for sale of goods exists is that a contract for sale of goods has certain peculiar features

compared to other types of contract, and so far as these features exist separate legal provisions are necessary. These separate legal provisions are embodied in the Indian Sale of Goods Act of 1930. The peculiar or special features of a contract for sale of goods may be set out as follows.

- (1) Contracts in general, as we have seen before, may be of various types, e.g. a promise in return for a loan, or a promise to do certain work in return for a counter promise, or a promise given or act done in return for a past act and so on. *But a contract for sale of goods is in every case a contract for sale of moveable property.*
- (2) The consideration for sale of goods is in every case money paid or agreed to be paid as a price.
- (3)) A contract for sale of goods involves in every case a transfer of the property in the goods to the buyer for a price.

#### **Contract for Sale of Goods :**

A contract for sale of goods has been defined by the Indian Sale of Goods Act as a contract whereby the seller transfers or agrees to transfer the property in goods to the buyer for a price. This definition thus involves

(1) A transfer of property in goods from the seller to the buyer. Property in goods means the right to own the goods, which right would be valid against the whole world. The right transferred must be the absolute or general property in the thing sold. When goods are delivered, for example, in pawn or pledge, the general property remains with the pawnor which he may transfer to a third person subject to the rights of the pawnee, and a special property is transferred to the pawnee. The pawnee cannot sell the goods, for he has only a special property, and in instance of special property can not constitute a sale.

(2) A transfer or an agreement to transfer property in goods. A sale takes place not only when there is an actual transfer of property in goods but also when there is an agreement to transfer such property in goods. A has a book. He transfers his right to B for Rs 5/- There is a sale. A agrees to transfer his right two months hence for Rs. 5/- There is a valid sale in this case also. An agreement to sell becomes a sale when the time elapses or the

conditions are fulfilled subject to which the property in the goods is to be transferred

(3) A sale of goods always means a sale of movable property. Goods means movable property and never include immovable property.

(4) The consideration for sale of goods is always a price in terms of money. Exchange of goods by buyer does not constitute a sale of goods.

#### **Formation of a Contract :**

A contract of sale is made in the same way as any other contract by an offer to buy or sell goods for price and the acceptance of such offer. The contract may provide for the immediate delivery of the goods or the immediate payment of the price or both or for the delivery or payment by instalments or that the delivery or payment or both shall be postponed. The contract may be in writing or by word of mouth or may be implied from the conduct of the parties.<sup>1</sup>

#### **Subject matter of a Contract :**

Goods, as we have already seen, form the subject matter of a contract of sale. Goods to be sold may or may not exist. I may sell cycles that are in my godown or I may agree to sell cycles which I expect to arrive from future goods. I might two months hence. I may even agree to sell goods which I shall acquire on the happening of a contingency, e.g. my father has got a few copies of Shakespeare's first editions. I hope to get them on my father's death. I may contract to sell them even before my father dies. Non-existent goods sold are called future goods. Future goods are defined as goods to be manufactured or produced or required by the seller after the making of a contract of sale. A sale of future goods is nothing but an agreement to sell the goods.

Where there is a contract for the sale of specific goods, the contract is void if the goods without the knowledge of the seller have, at the time when the contract was made, perished or become so damaged as no longer to answer to their description in the contract. This is a case of mistake.

Where there is an agreement to sell specific goods and subsequently before the risk passes to the buyer, without any fault of either the buyer or the seller, the goods perish or become so damaged as no longer to answer to their description in the agreement, the agreement is avoided.

**Risk attaching to the goods of** unless otherwise agreed, the goods remain at the seller's risk until the property therein is transferred to the buyer; but when the property therein is transferred to the buyer, the goods are at the buyer's risk, whether delivery has been made or not. Provided that, if loss ensues due to delay in delivery caused by either the buyer or the seller, the loss must be borne by the party who causes the delay. A sells 100 baskets of oranges to B. The property passes to B. But it is agreed that B must send his t<sup>o</sup> to carry the oranges. B fails to mind boats and the oranges are spoilt. B must bear the loss. Now let us suppose that instead of B, A was to have delivered the oranges. A fails to deliver. A must bear the loss.

### **Transfer of Property :**

We have already seen that a contract of sale of goods is a contract, whereby the seller transfers or agrees to transfer the property in goods to the buyer for a price. This means that the passing of property is the essential ingredient without which there can be no contract of sale. Property is a notional attribute inherent in goods which has the effect of vesting ownership in the person to whom property is transferred. It is, therefore, important to know when actually the property in good sold passes from the seller to the buyer. For this purpose we have first of all to understand the distinction between ascertained goods and unascertained goods.

Ascertained goods are those which are specific and ascertained, so that the identity of the goods is clearly understood and stand by the parties to a contract of sale. A says to B, 'I shall buy the blue glass jar which is placed on the window of your shop'. In this case both A and B know clearly the identity of the subject matter for

sale. But if a contract is merely for the sale of goods by description, such as a contract for the sale of a certain quantity of rice or of future goods, such as certain articles which are in the process of manufacture, the subject matter for sale is not identified and understood clearly by the parties. In such a case the contract is for sale of unascertained goods. Goods are unascertained even if the parties have agreed that they shall be taken from some specified buyer's stock such as a mound of rice from a particular godown containing 10 mds of rice.

### **Passing of property in ascertained goods :**

In the case of ascertained goods, the property in them passes to the buyer from the seller when the parties intend such property to be transferred. Such intention should be gathered from the form of the contract, the conduct of the parties and all the circumstances of the case. Unless a different intention appears from the form of the contract or the conduct of the parties or the circumstances of the case, the following rules should be followed for ascertaining the intention of the parties as to the time at which the property in the goods passes to the buyer.<sup>1</sup>

(a) In the case of a sale of ascertained specific goods in a deliverable state, the property passes to the buyer as soon as the contract is made provided that the contract is unconditional. Goods are said to be in a deliverable state when they are in such state that the buyer would, under the contract, be bound to take them. A contract of sale is said to be unconditional when it is not dependent on other factors. A buys a diamond of no end use that the sale will be effected if C approves. Here the contract is dependent on C's approval and is therefore not unconditional.

(b) When the specific goods are not in a deliverable state and the seller is bound to do something for the purpose of putting them into a deliverable state the property does not pass until such thing is done and the buyer has notice thereof. A buys a gold ring of B to be delivered when the ring is polished. The property in the ring would not pass to A until B's polishing

<sup>1</sup> Section 19 (1), (2) & (3)

<sup>2</sup> Section 20

the ring and put it into a deliverable state and A has notice thereof<sup>1</sup>.

(c) Where there is a contract for the sale of specific goods in a deliverable state, but the seller is bound to weight, measure, test or do some other act or thing with reference to the goods for the purpose of ascertaining the price, the property does not pass until such act or thing is done and the buyer has notice thereof<sup>2</sup>.

(d) When goods are delivered to the buyer on terms, e.g., "sale on approval" or "on sale or return" or other similar terms, the property therein passes to the buyer.

(i) When he signifies his approval or acceptance to the seller or does any other act adopting the transaction :

(ii) If he does not signify his approval or acceptance to the seller but retains the goods without giving the seller any notice of rejection, then, if a time has been fixed for the return of the goods, on the expiration of such time, and, if no time has been fixed, on the expiration of a reasonable time.

Let us illustrate the above. Thacker Spink & Co of Calcutta sends a copy of Galsworthy's For ye Sage to A at Dacca to be kept or returned within a fortnight on A's request to send a good book for approval. If A accepts the book and lets Thacker Spink & Co. know about it, the property in the book will at once pass to A. If A retains the book without informing Thacker Spink & Co. whether he wants to accept or reject the book, the property will pass to A after the expiry of a fortnight. If, however, no time was mentioned within which the book should be returned and A neither accepted nor rejected the book, the property in the book will pass to A on the expiry of a reasonable time. What is reasonable time will, of course, depend in every case on the general usage of the trade and all other circumstances of the case.

#### **Passing of property in unascertained goods :**

In the case of unascertained goods, property in them does not pass until they are ascertained<sup>3</sup>. B agrees to buy a glass from

<sup>1</sup> Section 21.

<sup>2</sup> Section 22.

<sup>3</sup> Section 18.

as godown. Property in the glass would not pass to b until he has selected his glass from all the glass in the godown. In accustomed word, all future goods though they may be spoken, are at same stage, for the purpose of determining the time at which property in them pass to the buyer should be remembered in his own case.

Where there is a contract in the sale of miscellanea<sup>1</sup>, future goods by description and goods of the description and are deliverable to the vendee fully prepared, the property passes by the seller with the set of the buyer and becomes with him on the day when it is handed over to him, unless there is to be buyer such a provision in the contract. There may be even other before the payment is made.

What happens if the vendor sells the goods to the buyer before the price is paid? The buyer (who is named by the vendor) takes the goods in full without having paid the price which has been agreed upon. He will be entitled to goods on the

### **Unconditional Appropriation :**

When the vendor in his contract specifies that he shall in some manner, so do or so shall act in fulfilment of the contract, it is to be the manner in which he contracts.

When he contracts to deliver under the contract he identified by him, i.e., the subject matter of the contract or he does nothing further remains to be done by the seller to give the property the property will pass to the buyer unless a contrary intention is expressed. It is the act of identifying the subject matter of it by itself is sent so that it may become clear as to in what the contract will attach which is known as unconditional appropriation. In Shukerdass Jyoti Prasad vs Bhinoram Shewdhal<sup>2</sup> the facts were as follows:

A contract of sale for 414 tuns of oil which were not at the

<sup>1</sup> Section 23 (1) & (2)  
- Mulla's Sale of Goods, p. 124

<sup>2</sup> (1925) 1ah 406

time of the contract in the possession of the seller was entered into by the parties on the 6th of May. The buyer paid the price at the time of the contract. Subsequent to the contract the seller got the Railway receipt for the goods despatched to the buyer earlier and endorsed the same and sent it to the buyer. Thereafter the goods were destroyed by fire while in transit. It was decided that the property had passed to the buyer as soon as the Railway receipt was sent to him and he had to bear the loss.

It should be noted, however, that the passing of property does not depend on the payment of the price or on the fact of delivery and property may pass from the seller to the buyer even if the seller refuses to deliver except on payment of price. For the right of the seller to retain property may be quite consistent with the transfer of property.

#### **Reserving the right of disposal:**

Where there is a contract for the sale of certain goods or where goods are subsequently appropriated to the contract, the seller may by the terms of the contract or appropriation reserve the right of disposal of the goods until certain conditions are fulfilled. In such a case, notwithstanding the delivery of the goods to a buyer or to a carrier or other bailee for the purpose of transmission to the buyer, the property in the goods does not pass to the buyer until the condition imposed by the seller is fulfilled.

Where the goods are shipped and by the Bill of Lading the goods are deliverable to the order of the seller or his agent, the seller is *prima facie* deemed to receive the right of disposal. Where the seller of goods draws on the buyer for the price and transmits the Bill of Exchange and the Bill of Lading to the buyer together to secure acceptance or payment of the Bill of Exchange the buyer is bound to return the Bill of Lading if he does not honour the Bill of Exchange and if he wrongfully retains the Bill of Lading the property in the goods does not pass to him.<sup>1</sup>

The above law is an exception to the rule that the property in the goods passes on appropriation of the goods to the contract on the principle that only in unconditional appropriation has the effect of passing the property. If the appropriation is condi-

<sup>1</sup> Section 25.

tional, then the seller retains the right of disposal, the goods and the property will not pass to the buyer unless the conditions of appropriation are fulfilled. The conditions may be of various types and the example afforded by Section 25 gives 3 paragraphs 2 & 3 above are merely illustrations. When a right of disposal is reserved by attaching the conditions to the contract it is said that the seller has reserved the right of disposal. The law regarding reserving the right of disposal has been laid down by Colton, L J in *Murphy v Imperial Automan Bank* as follows:

Under a contract for sale of chattels not specifying the place of delivery the property does not pass to the purchaser unless there is after delivery an appropriation of the specific chattels to pass under the contract, that is, unless both parties agree as to the specific chattels in which the property is to pass, and nothing remains to be done in order to pass it. If he is in default of such a contract he delivers by the vendor to a common carrier or (unless the effect of the shipment is restricted by the terms of the bills of lading) shipment on board a ship or a vessel chartered for the purchaser an appropriation sufficient to pass the property. If however the vendor, when shipping the articles which he intends to deliver under the contract, leaves the bill of lading in his own order and does no assignment on behalf of the purchaser but on his own behalf it is held that he thereby reserves to himself the power of disposing of the property and that consequently there is no final appropriation and the property does not on shipment pass to the purchaser. When the vendor on shipment leaves the bill of lading to his own order he has the power of absolutely disposing of the cargo and may prevent the purchaser from ever asserting any right of property therein. In accordance with *Witt v Biley*, *Hetherow v Magnier* and *Gubrium v Kieft* (in each of which cases the vendor had dealt with the bill of lading for their own benefit) the decisions were that the purchaser had no property in the goods though he had offered to accept bills for or had paid the price. So, if the vendor deal with or claims to retain the bill of lading in order to secure the contract

<sup>1</sup> (1978) 3 Ex D 164

<sup>2</sup> (1848) 2 Fx 1

<sup>3</sup> (1843) 6 Ex 570

<sup>4</sup> (1875) LR 10 Ex 274

price, as when he sends forward the bill of lading with a bill of exchange attached, with directions that the bill of lading is not to be delivered to the purchaser till the acceptance or payment of the bill of exchange, the appropriation is not absolute but until acceptance of the draft, or payment or tend to be conditional only, and until such acceptance or payment is tendered the property in the goods does not pass to the buyer, and so it was decided in *Turner v. Trustees of Liverpool Docks, Sheephead & Harrison Owners & Shutter* but if the bill of lading has been dealt with only to secure the contract price there is neither a right nor duty for holding, that in such case the goods shipped for the purpose of completing the contract do not on payment or tender by the purchaser at the contract price vest in him. When his cost there is no form of the condition subject to which the price will be paid, and nothing which according to the intention of the parties can serve to transfer the property done, obtain my opinion on such circumstances the property does not immediately tender the price to the purchaser.

In *Shepherd v. Harrison*<sup>1</sup> the facts were as follows:

The seller shipped a quantity of cotton from him at the risk of the buyer. The bill of lading was made over to the seller and was endorsed to the buyer with a full chain attached and sent to the buyer. The buyer paid the bill of lading but returned the bill of exchange. It was held that the property in the cotton did not pass to the buyer.

It is evident from what has said that the price does not necessarily pass to the buyer when the price is paid or the goods are delivered. The price may be paid before, after, or at the time the actual sale takes place. The Vauxhill Car Company are bringing out a special type of car. I anticipate that the demand for the cars will be so great that there will be hardly any car left in the market as soon as the car is placed on the market. I send the advertised sum of £150/- to Vauxhill Car Co. in advance on condition that as soon as the car will come in the market, the company will deliver me a car. The sale will be complete when the car will be delivered to me and not when



I have paid the price. In the same way, I may buy the car on credit and pay the price after the sale, or I may buy the car cash and pay the price at the time of the sale. Similarly, delivery may take place before, after, or at the time of the sale. I want to buy a typewriter. A firm sends me a typewriter to keep it if I buy it and return it in case I do not want to buy. If I buy the typewriter and pay the price, delivery would be before the sale or before the property passes to me. Similarly, I may buy the typewriter and pay the price first, and delivery of the typewriter to my house may take place later. Here property in the typewriter will pass to me immediately after I buy the typewriter, but the transfer of the possession of the typewriter takes place later. Delivery at the time of the sale is very common. In this case transfer of property and transfer of possession occur at the same time.

### **Passing of Title :**

The general law is that one who has no title to goods cannot himself give to another a better title. Therefore, if goods are sold by any one who is neither the true owner nor an agent of the owner authorised to sell, the buyer will acquire no title over the goods. In *Cundy vs. Lindsay*<sup>1</sup> the facts were as follows :—

One Alfred Blenkarn, writing from an address which he gave as 37, Wood Street, Cheapside, and signing his name, so that it looked like Blenkiron & Co., ordered some goods from the plaintiff. At 123 Wood Street were the premises of a reputable firm W. Blenkiron & Co. The plaintiff consigned the goods to Messrs Blenkiron & Co., 37 Wood Street, and Blenkarn obtained possession of them and re-sold to the defendants who bought in good faith. It was held that the defendants acquired no title as against the plaintiff. There are, however, some exceptions to this rule which might be stated as follows.

(a) **Estopel** : A buyer buying goods from one who is not the owner may still acquire a valid title, where, by the conduct of the owner, the buyer was led to believe that the seller was the true owner. B sells A's car to C. A was present at the sale. He keeps either silent or encourages C to buy the car. By his conduct C is led to believe that B is the owner of the car.

Here A, by his conduct, is estopped from denying B's authority to sell the car, and C acquires a perfectly valid title against A.

In *Commonwealth Trusts Ltd. vs. Akotey*<sup>1</sup> the facts were as follows :-

A sold a quantity of cocoa to B and consigned the same by railway and sent the railway receipts to B before any agreement was arrived at as to the price. B sold the cocoa to C and delivered the railway receipts to him. It was contended on behalf of A that, as there was no contract between A and B since the price was not fixed, the property in the goods did not pass to B and, therefore, C acquired no valid title. It was held that by his conduct A was estopped from disputing B's title to the cocoa and C had acquired a valid title.

(b) Sale by a mercantile agent : A mercantile agent is deemed in law to have the implied authority of his principal to sell his goods where the agent is in possession of the goods or the documents of title to the goods, with the consent of the principal. He can sell and pass a valid title to the buyer even where he had no authority to sell, provided the buyer did not know that and acted in good faith. This is also a special case of estoppel. The owner of the goods by giving possession of the goods to his agent impliedly leads the buyer to believe that the agent has authority to sell and he is, as such, estopped from denying the title of the buyer.

In *Folks vs. King* the facts were as follows -

The plaintiff handed over a motor car to a mercantile agent for sale on condition that the car should not be sold below a specified price. The agent agreed to do so but sold it below such price to A and misappropriated the proceeds. A bought the car in good faith and is sold it to the defendant. It was held that the plaintiff could not recover the car from the defendant.

(c) Sale by one joint owner : Where several persons are joint owners of goods and one of the joint owners is in possession of the goods with the consent of the other owners, the joint-owner who has possession of the goods can sell and pass a valid title to anyone who buys of him *in ignorance that the seller was only a*

<sup>1</sup> (1926) A.C. 72 P.C.

<sup>2</sup> Section 27.

<sup>3</sup> (1923) 1 K.B. 282 C.A.

*joint-owner and had no authority to sell.* Here also the other joint-owners, by putting the seller in possession of the goods, are estopped from denying the title of the buyer, as their conduct induced the belief in the buyer that the seller had a full authority to sell.

(a) Sale by person under void and voidable contracts : We have seen before that certain contracts are void and certain contracts are voidable. Void contracts are void from the outset and voidable contracts are valid until the party entitled to repudiate it actually avoids it.

A person who acquires goods on a voidable contract can pass a valid title to a buyer provided the same takes place before the contract is repudiated by the original seller. In *Phillips v. Brooks*<sup>1</sup> the facts were as follows.

A fraudulent person, North, entered into a jeweller's shop and looked at certain jewels which the jeweller was prepared to sell to him individually as a usual customer. North then drew a cheque in the name of Sir George Bullough, representing himself to be so, and took away one of the jewels. North then pledged the jewel with a pawn broker, who took it in good faith. It was held that the contract between the jeweller and North was not void but voidable though the jeweller believed North to be Sir George Bullough yet he intended to sell North and hence the contract was not void for mistake as to the identity of the party but voidable for fraud and misrepresentation. It was therefore decided that the pawn broker obtained a good title as he took the jewel before the jeweller repudiated the contract.

But a person who acquires the goods under a void contract cannot, at any time, pass a valid title to a buyer. A goes to a jeweller's shop and introduces himself say as Lord Halifax and induces the jeweller on such misrepresentation to let him have the jewel on credit. A sells the jewel afterwards to C. C. cannot have a valid title against the jeweller as the contract between A and the jeweller was void *ab initio* for mistake as to the identity of party.

(c) Seller in possession after sale : If the seller continues to be or is in possession of the goods or of the documents of title to

<sup>1</sup> (1919) 2 K.B. 243.

<sup>2</sup> *Lake vs. Simmons*, (1927), A.C. 487.

the goods for the sale, a subsequent buyer purchasing from such seller or from his agent acquires a valid title against the former buyer, provided he had no notice of the previous sale until he acted in good faith.

(f) Buyer in possession after sale. In the same way if a buyer is in possession of goods with the consent of the seller under an agreement that he can pass valid title to a third person who has no notice of the original seller's rights or heirs. This is illustrated by the case of *Hue, upon a Agreement*. A hirer purchases furniture on hire purchase by which the buyer gets possession of the goods immediately and the price is paid in several instalments. Until the entire price is paid the seller retains the ownership of the goods. But since the buyer is in possession of the goods he can pass valid title to a third person who buys the goods in good faith and with notice that the goods were subject to mere purchase agreement.

Sometimes a third party acts in whom is paid a regular interest by a hirer for the hire. I hire a radio from a shop and I pay R. L. is hirer to the hirer. In this case too possession is transferred to me. In fact the transaction actually looks like a hire purchase agreement. But I cannot pass valid title to a third person by selling the radio to him, for the transaction was not a hirer's contract for hire. It is stated change <sup>in</sup> <sub>in</sub>

### **Conditions and Warranties :**

We have discussed before how that subject of certain conditions are discharged due to non-fulfilment of those conditions. We also had a look at various stipulations to which contracts may be subject to not conditions<sup>1</sup>. A stipulation or a term relating to the subject matter of contract and in the case of sale of goods to the subject matter of sale may be either a condition or a warranty.

1. A *condition* is a term of the contract which goes so directly to the root of the contract or is so essential to its very nature that if the condition is not fulfilled the contract is discharged.

2. A *warranty* is a term of the contract which is independent

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<sup>1</sup> See ante under 'Law of Contract'.

and subsidiary or collateral to the main purpose of the contract, *i.e.*, which is not so essential as to discharge the contract in case the warranty is not fulfilled.

3. Whether a term is a condition or a warranty depends solely upon what was the intention of the parties. Let us take a simple case. A sells a car to B and says "It runs thirty miles per gallon of petrol." It turns out that the car does not run more than twenty-five miles a gallon. A statement is merely a warranty, for the parties never intended that the sale of the car would depend on the car running thirty miles per gallon. As statement was independent and collateral to the main contract of the sale. Therefore B is not entitled to repudiate the contract. He will have to keep the car. If he has paid the price, he may sue A for damages for breach of warranty. If he has not paid the price he can set up the breach of warranty as a deduction of the price. If on the other hand I had said "I will not sell the car unless it runs thirty miles per gallon" and A accepted. Yes it runs thirty miles per gallon the stipulation that he will run twenty-five miles per gallon would amount to a condition. B could then repudiate the contract if the car did not run thirty miles per gallon or refuse to take the car and recover the price if he had paid it, and sue A for damages for breach of contract.

But in some cases breach of warranty may amount to misrepresentation and the party injured by misrepresentation may always repudiate the contract. Let us return to side our first illustration. If A says to B first that the car runs thirty miles per gallon and then B buys the car it is natural to infer that A's statement induced B to enter into the contract. Therefore, if the car does not run thirty miles a gallon the breach of warranty will also amount to misrepresentation and B in such a case can repudiate the contract though the stipulation is not a condition.

It is, therefore, evident that the distinction between a *condition* and a *warranty* is important in so far as the rights of parties are concerned in case of a breach of either. A breach of condition, as we have seen above, entitles the injured party to avoid the contract, and sue the other party for damages for breach of contract. A breach of warranty, on the other hand, does not entitle the injured party to repudiate the contract. The injured party is only entitled to recover damages for the breach.

Where a contract of sale is subject to any condition to be

fulfilled by the seller, the buyer may waive the condition or elect to treat the breach of the condition as a breach of warranty and not as a ground for treating the contract as repudiated<sup>1</sup>. This means that the buyer can always dispense with the performance of a condition inserted in the contract for his sole benefit and treat the breach of condition as only a breach of warranty which entitles him to compensation. In some cases the buyer has to compulsorily waive a condition and to preclude himself from repudiating the contract as a result of a breach of condition, where he does something which is contrary to the seller's right to the property in the goods, such as when he resells the goods to a third party or exercises some right of proprietary character.

Where also a contract of sale is not separable, and the buyer has accepted the goods or part thereof, or where the contract is for specific goods the property in which has passed to the buyer, the breach of any condition to be fulfilled by the seller can only be treated as a breach of warranty and not as a ground for rejecting the goods and treating the contract as repudiated, unless there is a term of the contract expressed or implied to that effect. In the case of *Street v. Blake*, it was held that it is a well settled rule of English law that in the case of sale of specific goods, the buyer cannot repudiate the contract for non performance of a condition where the property in the goods has already passed to the buyer unless there is a stipulation in the contract cutting him to do so. The breach of condition in such a case is to be treated as a breach of warranty entitling the buyer to compensation only.

Conditions and warranties may be either express or implied. We have seen that conditions are illustrative implied conditions and warranties. They are in every case gathered from the intention of the parties and from all the express and implied language. In the case of sale of goods the implied condition is that there is no implied condition or warranty as regard the quality or fitness of goods sold. Unless the seller actually commits misrepresentation to induce the buyer to buy the seller is under no obligation to guarantee the quality.

<sup>1</sup> Section 13 (1)

<sup>2</sup> Section 13 (2)

<sup>3</sup> (1881) 2 B & Ad 456

<sup>4</sup> See ante 'Law of Contract.'

or fitness of the goods supplied. The buyer must look for himself and test the quality of goods he buys. The principle of *Caveat Emptor* applies<sup>1</sup>.

But the Sale of Goods Act provides for certain implied conditions and warranties unless there is any contract to the contrary :

#### Implied conditions :

1. There is an implied condition that in every case of sale the seller has a right to sell the goods, and in every case of agreement to sell, the seller will have a right to sell at the time when the property in the goods is to pass. This does not mean that the seller should be the owner of the goods. The seller might be an agent of the owner authorised to sell the goods.

In *Roland v. Vidoll*<sup>2</sup> the facts were as follows :—

The defendant sold a motor car to the plaintiff. After some time the plaintiff discovered that the car was stolen and he was compelled to return it to the true owner. It was held that the contract could be repudiated by the plaintiff for non fulfilment of the condition regarding title and he could recover the price from the defendant.

2. There is an implied condition that in a sale of goods by description, the goods shall correspond with the description; and if the sale is by sample, as well as by description, the goods shall correspond with both the sample and the description<sup>3</sup>.

It is not enough that the bulk of the goods correspond with the sample if the goods do not also correspond with the description. A contracts to sell B two sugar in accordance to the sample produced by him. The sugar which A delivered, agrees with the sample but is not fair sugar. In this case, although the goods agree with the sample, if they do not correspond with the description, and hence B, the buyer is entitled to reject the goods for non fulfilment of conditions. In *Nicol v. Go's*<sup>4</sup>, the facts were as follows :—

<sup>1</sup> See ante "Law of Contract."

<sup>2</sup> Section 14 (a)

<sup>3</sup> (1923) 2 K.B. 500 C.A.

<sup>4</sup> Section 15

<sup>5</sup> (1854) 10 Ex. 191

A sold a quantity of foreign refined rape oil warranted only to be equal to samples. The samples contained an admixture of hemp oil and the bulk corresponded with them. It was held that, though the oil was equal to sample, yet it did not correspond with the description, and hence the buyer was entitled to reject the oil.

3 Generally there is no implied condition as to the quality or fitness for any particular purpose of goods supplied under a contract of sale. The general law is "*Caveat Emptor*". But where the buyer makes known to the seller the particular purpose for which the goods are required, so as to show that the buyer relies on the skill and judgment of the seller, and such goods are normally sold by the seller, there is an implied condition that the goods will be reasonably fit for such purpose. I want a push chair for an invalid. I go to a shop where push chairs are *normally sold*. I tell the shopkeeper that the chair is needed to carry an invalid about. I also rely on the skill and judgment of the seller and ask him to give me a push chair fit for the purpose of carrying an invalid. Here if the shopkeeper sells a push chair to me there will be an implied condition that the push chair is fit for carrying an invalid about. But where a specific article is sold under its patent or other trade name there is no implied condition as to its fitness for any particular purpose.<sup>1</sup>

In *Chanter vs Hopkins*<sup>2</sup> the facts were as follows -

A placed an order with B for the latter's smoke consuming furnace to fit up with the former's brewing machine. The furnace was patented but it proved useless for the purpose of brewery. It was held that the buyer had no remedy against the seller as the goods were sold under its patent.

4 There is an implied condition in case of a sale by description that the goods shall be of merchantable quality. Provided the buyer has examined the goods there shall be no implied condition as regards defects which such examination ought to have revealed.

A sale by description means that a fair sketch or account of the goods is given by words or in writing.

In *Ptee Mohanmad vs Dalooram*<sup>3</sup> it was held that the condition regarding merchantability was broken where black yarn was

<sup>1</sup> Section 16(1)

<sup>2</sup> (1838) 4 M. N. W. 399

<sup>3</sup> Section 16(2)

<sup>4</sup> 47 C 555

sold by description and the same was found damaged by white ants.

In *Thurnett & Fehr vs. Beers & Sons*<sup>1</sup>, however, a buyer was given the inspection of certain barrels of glue which were not of merchantable quality. The buyer inspected the outside of the barrels only and if the barrels were opened it would have shown the condition of the glue. It was held that under the circumstances there was a breach of implied condition regarding merchantability.

5. Besides the implied conditions mentioned above, an implied condition as to the quality or fitness for a particular purpose may be annexed by the usage of trade to any contract of sale.

6. A contract for sale by sample means that the goods sold are fairly represented by the piece known as sample. It means that the thing sold is of "the same kind and as nearly of the same quality as the specimen which the seller showed to sample." In a contract for sale by sample there is an implied condition—*viz.*

(a) That the thing shall correspond with the sample in quality;

(b) that the buyer shall have a reasonable opportunity of comparing the bulk with the sample;

(c) that the goods shall be free from any defect, rendering them unmerchantable which would not be apparent on reasonable examination of the sample. In *Mody vs. Gregson*<sup>2</sup> the defendants agreed to manufacture and supply 2500 pieces of grey shirting according to sample at 18s 6d per piece each piece to weigh seven pounds. The goods were delivered and the plaintiff accepted them as in accordance with the sample. But it was found later that the goods contained china clay to the extent of 15 per cent of their weight introduced for the purpose only of making them weigh seven pounds. It was held that the defect could not be apparent on reasonable examination of the sample and as such the implied condition regarding merchantability was broken.

*Implied Warranty* (1) In a contract of sale there is an implied warranty—

(a) that the buyer shall have and enjoy quiet possession of the goods. This means that the seller must pay damages for

<sup>1</sup> (1919) 1 K.B. 486.

<sup>2</sup> Section 16 (3).

<sup>3</sup> L.R. 4 Ex. 49.

**breach of warranty if the buyer suffers from the consequences of a defective title;**

(b) That the goods shall be free from any charge or encumbrance in favour of any third party not declared or known to the buyer before or at the time when the contract is made.

(2) An implied warranty as to quality or fitness for a particular purpose may be annexed by the usage of trade. Thus in *Jones v. Bowden*<sup>1</sup> it was shown that in auction sales of certain drugs, as pigments, it was usual to state in the catalogue whether they were sea-damaged or not, and in the absence of a statement that they were sea-damaged, they would be assumed to be free from that defect. Fair samples had been shown, but sea-damage could not be detected by examination. The court held, on this evidence, that freedom from sea-damage was an implied warranty in the sale.

#### **Rights and duties arising out of a contract of sale :**

The Indian Sale of Goods Act confers certain rights and duties on the buyer and the seller respectively. Since the buyer and the seller are the only two parties in a contract of sale, it is easy to understand that what is the right of the buyer is actually the duty of the seller, and what is the right of the seller is actually the duty of the buyer. Therefore we shall deal with the rights of the buyer (*i.e.*, the duties of the seller) first and deal with the rights of the seller (*i.e.*, the duties of the buyer) next.

#### **Rights of the buyer :**

The rights of the buyer may be enumerated as follows :

**Right of the buyer regarding delivery :** It is the duty of the seller to deliver the goods and of the buyer to accept and pay for them in accordance with the terms of the contract of sale<sup>2</sup>.

**Delivery** Unless otherwise agreed, delivery of the goods and payment of the price are concurrent conditions, that is to say, the seller shall be ready and willing to give possession of the goods to the buyer in exchange for the price, and the buyer shall be ready and willing to pay the price in exchange for possession of the goods<sup>3</sup>.

Delivery of goods sold may be made by doing anything which,

<sup>1</sup> (1903) 1. K.B. 610

<sup>2</sup> Section 31

<sup>3</sup> Section 32.

**Delivery how**      he or a agent shall be entitled as deliver or made which has the effect of putting the goods in the possession of the buyer or of any person authorised to hold them on his behalf. Even the handing over of the key can only be agreed to as a delivery of the car<sup>1</sup>.

'A delivery or put of good in progress of the delivery is the whole has the same effect for the purpose of passing the property in such goods as a delivery of the whole, but

**Put delivery**      such as a part of the goods with an intention of removing it from the whole does not operate as

delivery of the remainder. The intention of severing the part from the whole is to be inferred from the facts and circumstances of the case. A sells 1 ton of coal to B. As lorry can carry only one ton at a time. Such delivery is a part. This in progress of delivering the rest. The delivery one ton will operate as delivery of the 1 ton. Let us suppose A delivers one ton to C and the rest to D. It is so his intention also with regard to be remaining 2 ton. In delivery of the next ton of coal this will be operating a delivery of the whole lot is As intention is to sever one ton from the rest.

#### **Rules as to delivery:**

In contract of sale the contract can always provide as to whether the seller should deliver or the buyer should take posse

or whether the goods are to be delivered at  
**Place of delivery**      a particular place or at the place where the sale took place. As it is in any such contract goods sold are to be delivered at the place at which they are at the time of the sale, and unless it is agreed to be sold it is to be delivered at the place at which they are at the time of the payment. All is it not then no existence of the place at which the goods mentioned are produced.

The seller of goods is not bound to deliver them until the buyer applies for delivery until there is a contract to the buyer<sup>2</sup>.

**Time of delivery**      In case of the goods to the buyer but no time for sending them is fixed the seller is bound to send them within a reasonable time. When the buyer demands delivery or when

<sup>1</sup> Section 33

<sup>2</sup> Section 34

<sup>3</sup> Section 36

<sup>4</sup> Section 35

<sup>5</sup> Section 36(2)

the seller tender delivery, such demand or tender must be done at a reasonable hour. What is reasonable hour is a question of fact<sup>1</sup>.

Where a seller sells goods which are in the possession of a third person there is no delivery by seller to buyer unless and until such third person of third persons deliverables to the buyer that he holds the goods on his behalf.

The expenses of and incidental to putting the goods into a deliverable state is to be borne by the seller unless there is an agreement to the contrary.

Where the seller delivers to the buyer quantity of goods less than he contracted to sell the buyer may reject them but if the buyer accepts delivery he has to pay for them at the contract rate. Where the seller delivers to the buyer a quantity of good larger than he contracted to sell the buyer may accept the goods included in the contract and reject the rest or he may reject the whole. If the buyer accept the whole of the good so delivered he will pay for them at the contract rate. Assume A contracts with B at Rs 4/- per ton. A however delivers only 8 tons. B can reject the delivery. But if B accept delivery he must pay for the 8 tons at the contract rate of Rs 4/- per ton, i.e. he must pay Rs '2' in all. But suppose A delivers 12 tons instead of 8 tons as above. Here B can keep 10 tons out of the 12 tons as the quantity fixed in the contract and reject the remaining two tons or B can reject the whole quantity or B can accept the whole of the 12 tons in it, however B accepts the whole of the 12 tons B must pay at Rs 4/- per ton i.e. he must pay Rs 48/- in all.

The seller may, instead of delivering a smaller or a larger quantity, deliver to the buyer the goods he contracted to sell mixed with goods of different description not included in the contract. In such a case the buyer may accept the goods which are in accordance with the contract and reject the rest or may reject the whole. All these rules may however be varied by any usage of trade, special agreement or course of dealing between the parties<sup>2</sup>.

<sup>1</sup> Section 36(4)

<sup>2</sup> Section 36(3)

<sup>3</sup> Section 36(5)

<sup>4</sup> Section 37

**Generally,** in the absence of any contract, the buyer of goods is not bound to accept delivery of them by instalments. But there may be contracts where delivery by instalments may be stipulated.

Where there is a contract for the sale of goods to be delivered by stated instalments and instalment to be paid separately, a difficult question arises in each of the following two cases:

(a) If the seller makes no delivery or makes a defective delivery in respect of one or more instalments, the question in this case is whether it is to be regarded that the seller has broken the whole contract, whether the breach is respect of the delivery of one or more instalments or is he separated from the contract and treated as a partial breach. Whether it is a breach of the whole contract or only of part of it, the right to rescission or fulfilment will depend on the terms of the contract and all the circumstances of the case. It would depend on the consideration of the whole point whether or not the contract is repudiated. If however the buyer only accepts the goods to buy in part and puts them to his use, it is only a partial breach. He can only claim damages for partial breach.

(b) If the buyer rejects or refuses to take delivery or pays for one or more instalments, this involves a question in each case as to what on the face of the contract and the circumstances of the case, if the rejection of one or more instalments is a repudiation of the whole contract, because it is a partial or a severable breach which is irreducible in proportion only but not to a right to set the whole contract as repudiated.

Where in pursuance of a contract of sale, the seller is required or required to send the goods to the buyer, delivery of the goods to a carrier whether named by the seller or by the buyer or not for the purpose of transmission to a wharfinger, the buyer or delivery of the goods to a wharfinger for sale custody is *prima facie* deemed to be a delivery of the goods to the buyer.

In the absence of any contract between the buyer and the seller, the Sale of Goods Act lays down the following rules as to who should bear the loss in case goods are damaged during transit from the seller to the buyer.

(a) Where goods are delivered to a carrier for transmission to the buyer (as stated above) or deposited with a wharfinger for safe custody, the seller must make such contract with the carrier or wharfinger on behalf of the buyer as may be reasonable having regard to the nature of the goods and the other circumstances of the case. If the seller omits to do so and the goods are lost or damaged in course of transit or whilst in the custody of the wharfinger, the buyer may decline to treat the delivery to the carrier or the wharfinger as a delivery to himself or may hold the seller responsible for such loss or damage.<sup>1</sup>

(b) Where goods are sent by the seller to the buyer by a route involving sea transit in circumstances in which it is usual to insure the seller must inform the buyer of goods so that the latter may insure in time. If the seller fails to inform and the buyer does not insure the seller must bear all the loss incident to the transit.

(c) Where the seller agrees to deliver the goods at his own risk at a place other than that where they are when sold the buyer must nevertheless make otherwise agreed take my risk of *deterioration* in the goods incident to the transit. Here the risk referred to is only the risk of deterioration and not of total loss. If the goods are totally lost the seller must bear the risk.

Where goods are delivered to the buyer which he has not previously examined, he is not deemed to have accepted them unless and until he has had a reasonable opportunity of examining them for the purpose of ascertaining whether they are in conformity with the contract. The seller is bound to afford to the buyer a reasonable opportunity of examining the goods for the purpose of ascertaining whether they are in conformity with the contract unless otherwise agreed. If the buyer does not examine the goods despite of reasonable opportunity being given by the seller the buyer is deemed to have accepted the goods.<sup>2</sup> The buyer is deemed to have accepted the goods when he intimates to the seller that he has accepted them or when the goods have

<sup>1</sup> Section 39 (2)

<sup>2</sup> Section 39 (3)

<sup>3</sup> Section 40

<sup>4</sup> Section 41

been delivered to him and he does any act which is inconsistent with the ownership of the seller, e.g. when he sells the goods to a third person, or when after the lapse of a reasonable time he retains the goods without intimating to the seller that he has rejected them<sup>1</sup>.

Unless otherwise agreed where goods are delivered to the buyer buyer not bound and the buyer refuses to accept them the buyer to return rejected is not bound to return the goods to the seller goods. But the buyer in such a case must inform the seller of his refusal to accept.

### Rights of the Seller :

(1) The seller is entitled to payment of the price at the same time as he delivers the goods unless otherwise agreed.

If the buyer fails to pay the seller can always sue for the price.

(2) The seller entitled to compensation if the buyer refuses to accept delivery of the goods sold.

(3) The seller is entitled to reasonable rate of interest on the total price of the goods sold from the day of the delivery of the goods or from the day on which the price was to have been paid.

### Unpaid Seller :

A seller of goods is become<sup>2</sup> an unpaid seller

(1) when the value of the price has not been paid or tendered or

(2) when a bill of exchange or other negotiable instrument, e.g., a cheque, has been accepted by the seller as conditional payment and the condition on which it was accepted has not been fulfilled by reason of the destruction of the instrument or otherwise. A sells 1 mrd. of rice to B for Rs 37. B pays Rs 5 by cheque. A accepts the cheque A accepting mean that he accepts payment of the price for 1 mrd. of rice on condition that the cheque will be paid. If the cheque is dishonoured A will become an

<sup>1</sup> Section 42

<sup>2</sup> Section 43

<sup>3</sup> Section 32

<sup>4</sup> Section 56

<sup>5</sup> Section 61

<sup>6</sup> Section 45 (1)

**unpaid seller.** A seller includes any person who is in the position of a seller, e.g. an agent of the seller to whom the bill of lading has been endorsed<sup>1</sup>.

### **Unpaid Seller's Rights :**

- (1) An unpaid seller has the following rights notwithstanding that the property in the goods may have passed to the buyer
    - (a) He has claim on the goods for the price while he is in possession of them
    - (b) He has right of stopping the goods in transit after he has parted with the possession of them in case of the insolvency of the buyer
    - (c) He has a right to resell the goods in some cases as defined by the Sale of Goods Act
    - (d) He can sue for the price
  - (b) An unpaid seller has the following rights when he has parted with either all the risks or some of the risks in the goods
    - (a) He is entitled to require payment before delivery
    - (b) He has a right of reholding delivery until concurrently with his rights of lien, he gets paid him + where the goods have been sold on credit
- Let us discuss each of the rights separately.

### **Seller's Lien :**

(1) Lien means a right exercised by one owner over another's property. A seller's lien arises therefore only when he property in the goods passes to the buyer. A seller can claim that an unpaid seller who is in possession of the goods till it is paid who he used to be the owner of such goods is entitled to retain possession of them until payment or tender of the price in the following cases<sup>2</sup>—

- (a) Where the goods have been sold on cash basis and without any stipulation is to credit. A sells 50 bushels of wheat to B for £30/- to be paid cash. B fails to pay. A can retain the wheat.
- (b) Where the goods have been sold on credit, but the term

<sup>1</sup> Section 45 (2)

<sup>2</sup> Section 46

<sup>3</sup> Section 56

<sup>4</sup> Section 47

I credit to the period during which such insurance is in force, he has paid 50% of the premium on credit, provided that the premium is paid within three months. The term of credit will expire on the 1st January 1911, and I shall assess on him the whole amount due on credit.

Siebenundfünfundvierzigster Tag  
des zweiten Monats im Jahr des Heiligen  
Friedrich Augustus, König von Sachsen.  
Von der Universität zu Leipzig.

(1) He said in a whisper at twilight as he was going to bed.

I am in no condition  
to do it to  
himself when the  
time comes  
I will see  
that he is not  
hurt.

July 1st 1871 in A.D.  
In the County of Middlesex before Richard G. Dyer Esq.  
Judge of the Probate and Orphan Court of Middlesex  
on the complaint of the above named Plaintiff against  
the defendant Wm. Chamberlain Esq. in the  
cause was delivered Wm. G. Dyer Wm. Chamber-  
lain and the appellants to hold the sum of the  
sum sold which was still in their warehouse at a sum of  
price It was held that the appellants were entitled to recover the  
sum in spite of the fact that the tea was混同with them in  
the capacity as binders for the respondent

**1 Section 49**

2 (1894) 8 Bon 501

**2 (1877) 3 AC 390 PC**

As has been noticed already the seller's lien is an incident of his possession, and hence the seller loses his lien as soon as he gives the buyer possession and his only remedy for the unpaid price in that event is to sue the buyer for the price of the goods and he cannot rely on any rights on the goods superior to those of any other creditor<sup>1</sup>.

### **Termination of lien :**

An unpaid seller loses his lien in the following cases :-

(a) When he delivers the goods to a carrier or other bailee for the purpose of transmission to the buyer without reserving to himself the right of disposal of the goods. A sells 50 apples to B for Rs 10/- A delivers the apples to a Rulw v Company for transmission to B. He further takes out the Rulw receipt in the name of B as he consents not to the receipt to B. Here A does not reserve the right of disposal. Hence he cannot retain the apples lying in the Rulw god with B till to pay the price subsequently but if A takes the Rulw receipt in his own name he could have claimed the apples as the receipt would indicate that he has reserved the right of disposal.

(b) When the buyer or his agent *lawfully* obtains possession of the good. A sells a car to B for Rs 2000/- B gets on the car and drives the car to his own garage before he has paid the price. Here A cannot retain the car as B has taken possession of the car *lawfully*. But suppose B wants to take the car to his own garage A objects and demands payment of the price before P takes the car home. B pushes A down and drives the car to his own garage. Here A cannot retain the car as B has taken possession of the car *lawfully i.e.* by using force.

(c) When the seller agrees with the buyer either expressly or impliedly that he would not exercise his right of lien. Such an agreement amounts to a waiver, i.e. renunciation of the seller's right of lien.

### **Stoppage in transit :**

A (a) The right of stoppage in transit is a right given to

<sup>1</sup> *Moncky Pestonji v. Wadilal Salabhai & Co.*, 53 I.A. 92.

the unpaid seller for regaining his possession of goods which he has parted with and which are in course of transmission but which have not reached the hands of the buyer or his agent in case the buyer becomes insolvent. The principle is stated in Section 50 of the Indian Sale of Goods Act in the following terms:

Subject to the provision of this Act when the buyer of goods becomes insolvent, the unpaid seller who has parted with the possession of the goods, has the right of stopping them in transit if it is to say, he may resume possession of the goods as long as they are in course of transit and may return them until payment or tender of the price. It should be noted that insolvency of the buyer does not mean that the buyer should actually be adjudged an insolvent. Insolvent has been defined in Section 2 (8) as follows:

A person is said to be insolvent who is unable to pay his debts in the ordinary course of business or cannot pay his debts as they become due whether he has committed an act of insolvency or not.

Thus the evidence of general inability to pay debts is enough to constitute a valid claim for the exercise of the right of stoppage in transit.

The right of stoppage can be exercised so long as the goods remain in the possession of the carrier. Whenever there is dispute as to the delivery of the goods, it is whether at the time of delivery the carrier by the vendor, the transit of the goods had or had not commenced. The relevant rule in S. 51 of the Sale of Goods Act is as follows:

(1) Goods are deemed to be in course of transit from the time when they are delivered into the care of the carrier for the purpose of transmission to the buyer until the buyer or his agent in its behalf takes delivery of them in such caravans or other bales. The transit comes to an end in case the buyer or his agent takes delivery from such caravans or bales. But the taking of delivery must be done as in act of carriage. The mere touching or handling of the goods without an intention to exercise the right of ownership will not terminate the transit. In *James v. Griffin*, the facts were as follows. Goods were consigned to buyer by a ship and the buyer became insolvent. The buyer under pressure from the captain sent his son to take the goods with definite

instructions not to meddle with the goods. The son had the goods landed at the wharf where they were stopped by the sellers. It was held that the taking of the goods by the son was not in effect ownership and the sellers were entitled to stop.

(2) If the buyer or his agent in that behalf obtains delivery of the goods before their arrival at the appointed destination in transit as it may be. The law on this point is clearly explained in *Buon Parte v. Whitchurch*. And is set out in the following words:

The law is clearly settled that if the buyer or his agent retakes the goods before he has arrived at the destination originally contemplated by the parties or makes in the meantime they have come into the control of constructive possession of the vendor. If the vendor takes them out of the possession of the carrier into his own before arriving, either without the consent of the carrier there exists a doubt as to whether it could be so done. This is a case of constructive possession. A case of constructive possession is where the carrier can expressly or by implication intend to have a claim arising from the original owner to come to hold the goods in the name of his agent not for the purpose of expediting them to the place of original destination pursuant to the contract but in a new character for the purpose of safety and account and subject to some new authority to be given to him.

(3) If, after the arrival of the goods at the appointed destination the carrier or other holds acknowledges to the buyer or his agent but he holds the goods in his behalf and continues in possession of them as bailee for the buyer or his agent, the transit is at an end and it is immaterial that a further destination for the goods may have been indicated by the buyer. This is a case of constructive delivery of the buyer. For the purpose of determining whether the transit has come to an end it is important to consider, even if the goods are still lying with the carrier or bailee, if the carrier or bailee is holding the goods as the agent of the buyer or not. If the carrier or bailee holds the goods as the agent of the buyer the transit comes to an end. It was said in *Richardson v. Goss*. If a consigne be in the habit of, with the consent of

the owner, using the warehouse of a carrier, packer, wharfinger, or other person as his own, for instance, by making it the repository of his goods, and disposing of them there, the transit will be considered as at an end when they have arrived at such warehouse."

(4) If the goods are rejected by the buyer and the carrier or their bailee continue in possession of them he transit is not deemed to be at an end even if the seller has refused to receive them back.

(5) When goods are delivered to a ship chartered by the buyer it is a question depending on the circumstances of the particular case whether they are in the possession of the master or a carrier or is agent of the buyer. The decision establishes the principle that if the seller delivers the goods to the master on board the ship is the agent of the buyer the transit comes to an end. But if the goods are delivered to the master of the ship chartered by the buyer only as a carrier the transit does not come to an end. In *Statesman v. Lincolnshire and Yorkshire Ry Co*<sup>1</sup> the facts were as follows. The seller delivered the goods on board ship before the buyer's agent employed as a general trader. The bills of lading were made out in the name of the buyer. It was held that the transit had come to an end by such delivery and the seller was precluded from stopping the goods. On the other hand, in *Ex parte Rosevear Chain Clly Co* the facts were as follows. The seller delivered goods on board a ship chartered by the buyers. The destination was not known and no bills of lading were made out. It was held that the transit had not come to an end. The distinction is clear. In the latter case the goods were only delivered to a carrier whereas in the former the goods were given to an agent of the buyer and delivery to the agent is delivery to the buyer.

(6) Where the carrier or other bailee wrongfully refuses to deliver the goods to the buyer or his agent in this behalf the transit is deemed to be at an end. In *Bird v. Brown* the facts were as follows. A gave notice to a carrier to stop the goods. A had no authority to give such notice, he being neither the seller nor his agent. Subsequently the assignee of the insolvent buyer

<sup>1</sup> L.R. 2 Ch App 332

<sup>2</sup> 11 Ch D 360

<sup>3</sup> 4 Ex 796

demanded the goods. The carrier refused to deliver the goods and handed them over to A. It was held that the stoppage was ineffective and the transit had come to an end on the wrongful refusal of the carrier to deliver the goods to the buyer's assignee. On the other hand if the right to stop is duly exercised the carrier must comply with it and he will be liable in damage if he wrongfully refuses.

(7) Where part delivery of the goods has been made to the buyer or his agent in that behalf, the remainder of the goods may be stopped in transit, unless such part delivery has been given in such circumstances as to show an agreement to give up possession of the whole of the goods.

#### **Right of Re-sale :**

A (m) The exercise by the unpaid seller of his right of lien or stoppage in transit as explained above does not *ipso facto* terminate the contract of sale. The contract of sale still subsists. The exercise of these rights is only intended to compel the buyer to pay the price which is incident to the contract of sale. But this does not mean that the unpaid seller has to wait *ad infinitum* to realise the price from the buyer. He can re-sell the goods and put an end to the contract of sale under the following conditions<sup>1</sup>:

(a) Where the goods are of a perishable nature, the seller cannot gain by just retaining the goods or stopping them in transit, for the goods may perish before long. In such a case, the seller is entitled to re-sell the goods. If the seller suffers loss on re-sale due to a fall of price, the buyer must make good the loss. If the seller makes a profit on a sale he is entitled to keep the profit. Added to this, the seller can sue the buyer for breach of contract.

(b) Where the goods are not of a perishable nature, the seller is entitled to re-sell the goods, provided he gives notice to the buyer of his intention to re-sell and the buyer fails to pay or tender the price within a reasonable time from the giving of such notice. The seller is also entitled to recover from the buyer any loss occasioned by the re-sale and to keep the profits, if any, on the re-sale. The seller is also entitled to sue the buyer for breach of contract. If, however, the goods are not perishable, or the seller sells non perishable goods without notice, the seller is not entitled to recover from

<sup>1</sup> Section 54

the buyer any loss he might suffer on the re-sale, and the profit on the re-sale, if any, will go to the buyer.

(c) Where the seller, at the time of the contract, reserves the right to re-sell in case the buyer defaults to pay the price, the seller can always sell the goods.

### Breach of Contract of Sale :

A contract of sale may be broken either by the buyer or the seller. The remedies for breach of contracts of sale are similar to the remedies of action upon contract or specific performance which we have studied in connection with breach of contract in general. We may enumerate the following remedies for typical breaches of contracts of sale:

(1) Where under a contract of sale the property in the goods has passed to the buyer and the buyer wrongfully neglects or refuses to pay for the goods according to the terms of the contract, the seller may sue him for the price of the goods.<sup>1</sup>

(2) Where under a contract of sale the property in the goods has not passed to the buyer, but according to the contract the price is to be paid on a certain day irrespective of delivery, the seller can sue the buyer for the price if the buyer refuses or neglects to pay the price on or before the appointed day.

(3) Where the buyer *wrongfully* neglects or refuses to accept delivery and pay for the goods, the seller may sue him for damages for non-acceptance. *But the word 'wrongfully'* <sup>2</sup> The buyer can refuse to take delivery if the goods are defective or not according to sample or description or if delivery is made for any other reason which is contrary to the terms of the contract. But the buyer cannot refuse to take delivery if the goods are delivered according to the terms of the contract. If he refuses he is deemed to do so unlawfully and in such case he is liable to damages for non-acceptance.<sup>3</sup>

(4) Where the seller *wrongfully* neglects or refuses to deliver the goods to the buyer, the buyer may sue the seller for damages for non-delivery. *But the word 'wrongfully'* here means that the seller cannot refuse to deliver the goods up to the buyer.

<sup>1</sup> Section 55 (1)

<sup>2</sup> Section 55 (2)

<sup>3</sup> Section 56

buyer has broken some terms of the contract, e.g., failure to pay the price on an appointed day. If the seller does so, he is deemed to have acted unlawfully and he will be liable to pay damages for non-delivery<sup>1</sup>.

(5) Where the seller is ready and willing to deliver the goods and the buyer neglects or refuses to take delivery even after a request from the seller, the buyer is liable to the seller for any loss occasioned by his neglect or refusal to take delivery and custody of the goods.<sup>2</sup>

(6) In some cases the court may compel the seller to deliver the goods and complete the sale by a decree of specific performance where the seller refuses to deliver the goods to the buyer. But the buyer can never be compelled to buy the goods where he refuses to accept delivery. A decree of specific performance will only be granted where ordinary damages for non-delivery will not sufficiently compensate the injury suffered by the buyer. The following illustration will make this clear. A contracts with the Government Supply Department to supply shells for guns. The manufacture of shells requires certain chemicals which is stocked only by B. A contracts with B for the purchase of the chemicals. Later on, B refuses to deliver the chemicals. Here damages for non-delivery will hardly compensate the loss which A will suffer for non-delivery of the chemicals. A wants the chemicals and money. In such a case, therefore, the court will compel B to deliver the chemicals by a decree of specific performance<sup>3</sup>.

(7) Where there is a breach of warranty by the seller, the buyer may

(a) set up against the seller the breach of warranty diminution or extinction of the price; or

(b) sue the seller for damages for breach of warranty<sup>4</sup>.

(8) Where either party to a contract of sale repudiates the contract before the date of delivery, the other may either treat the contract as subsisting and wait till the date of delivery, or may treat the contract as rescinded and sue for damages for breach<sup>5</sup>.

<sup>1</sup> Section 57.

<sup>2</sup> Section 44.

<sup>3</sup> See ante "Law of Contract" for specific performance.

<sup>4</sup> See ante "Law of Contract" on anticipatory breach of contract.

## CHAPTER III PARTNERSHIP

(*Indian Partnership Act*)

Partnership has been defined by the Indian Partnership Act<sup>1</sup> as the relation between persons who have agreed to share the profits of a business carried on by all or any one of them acting for all. Persons who have entered into partnership with one another are called individually partners and collectively 'a firm', and the name under which their business is carried on is called the 'firm name'. This definition means that to constitute a partnership the following conditions must be satisfied.

- (1) There must be a business.
- (2) There must be more than one man associated with the business. There cannot be however, more than twenty persons and in the case of a banking firm more than ten persons.
- (3) There must be a contract or agreement between the persons by virtue of which the persons are associated with the business.
- (4) The object of the business must be the earning of profit.
- (5) The business must be carried on by all or by any of them on behalf of all.

We may take a few illustrations to show that if any one of the above conditions is not satisfied, a partnership can not exist.

(a) A, B and C buy a few houses together as joint-owners. They collect the rent and share it between themselves. The relation between A, B and C is not one of partnership, for there is no business with which they are associated. A, B and C are simply co-owners of the houses.

(b) A, B and C jointly start a few stores in Calcutta to sell x-dustries and clothing to orphans and widows at cost price. As the object of the business of A, B and C is purely philanthropic & not to earn any profit A, B and C will not be deemed partners.

<sup>1</sup> Section 4

### Mode of Determining the existence of Partnership :

To determine whether a group of persons does or does not form a partnership or whether a person is or is not a partner in a firm, we have to consider the real relation between the parties as shown by all relevant facts taken together<sup>1</sup>. The Partnership Act lays down the following rules to assist the determination of the existence of partnership.

(i) Co-ownership — Partnership should be clearly distinguished from co-ownership. Co-ownership simply connotes the ownership of any particular thing being vested in more than one person whereas partnership always signifies the association of more than one person in a business with a common purpose, namely, the sharing of profits, and along with it, of losses.  
 'No one ever suggested that co-owners of a house let to a single tenant for example, i.e., one, either is to the house or is to the rent. Their shares are distinct, independent and separately transferable. If they used the house as a hotel managed by themselves or their agent for their common profit they would be partners in the business of hotel keeping.'<sup>2</sup> Thus it has been held that joint owners of a ship are not necessarily partners. But if the owner manage the ship in a commercial venture they constitute themselves as partners.<sup>3</sup>

(ii) The sharing of gross returns arising from property by persons holding a joint or common interest in that property does not of itself make such persons partners. This will be illustrated by the case of Lyon vs Knowles. The facts of the case were that the proprietor of a theatre hall let the hall to a man named Dillon. Dillon produced shows managed the theatre and paid all the expenses. The proprietor of the hall paid for only a few minor expenses. The arrangement between the proprietor and Dillon was

<sup>1</sup> Section 6.

<sup>2</sup> Pollock & Mulla—Indian Partnership Act—p. 9

<sup>3</sup> Helwe *vs* Smith. (1831) 7 Bing. 709.

<sup>4</sup> Green *vs* Brigg. (1847) 6 H. 395

<sup>5</sup> (1863) 3 B. & S. 1.

that the proprietor would collect all the box money and appropriate half of it. In the light of these facts the court found that the proprietor of the hall shared no risk incidental to the running of the shows with Dillon. He simply took half of the box money as payment for the use of the hall. He did not share net profits but only gross profits and is such was not a partner with Dillon.

(ii) The sharing of profits arising from property by persons holding a joint or common interest in that property, or the sharing of the profits of a business by Partnership Act lays down the following exceptions. Lewis le Flam v. v. Leclercq<sup>1</sup> held that although right to participate in profits is a strong test of partnership, though there may be cases where from such participation alone it will be inferred yet if the other factor does not exist may depend on the real intention and conduct of the parties, and not upon this one term of it which provides for the participation in profits. The Partnership Act lays down the following exceptions specifically where the sharing of profit does not constitute a partnership.

(a) Where a lender lends money to persons engaged in business or about to engage in business, and receives payment by instalments out of the profits of the business, the lender shares profits but does not thereby become a partner.

(b) When a widow or a child gives remuneration on the basis of profits of business which she runs, but shares profits but does not thereby become a partner.

(c) Where the widow or child of a deceased person is given an annuity out of the profits of the business, the widow or child shares profits but does not become a partner.

(d) Where the seller of a business shares profit out of the business in consideration of the sale of that business such seller shares profits, but he does not, thereby, become a partner.

<sup>1</sup> (1860) 8 H.L. Cases 268, 36 Digest 528, 91  
<sup>2</sup> Underhill.

### **Creation of Partnership :**

A partnership is brought into existence by agreement or contract between persons who agree to become partners in a business. This agreement need not be in writing and the terms of partnership may be proved by oral evidence or even inferred from the course of dealing of the parties. But generally, where the business is large, the partnership contract is reduced into writing and very generally the terms are embodied in a deed. This deed is known as the articles of Partnership. The articles generally contain the following particulars :

1. The name of the firm.
2. The nature of the business.
3. The duration of the partnership where such duration is fixed.
4. The management of the business.
5. The keeping of accounts.
6. The authority for signing cheques.
7. The provision as to the death or retirement of a partner.
8. The keeping and examination of accounts.

### **A partnership and a Joint Hindu Family business :**

Sec. 5 of the Partnership Act declares that the members of a Hindu undivided family carrying on a family business as such, or a Burmese Buddhist husband and wife carrying on business as such, are not to be regarded as partners in such business. The points of difference between a partnership and a joint Hindu family business may be set out as follows :—

(1) Partnership can only be created by contract. When several persons agree to join each other in a partnership business a partnership is born. But a joint Hindu family business is not the creation of contract. Persons become members of a joint family business because they are born in a joint family which happens to own a business. Membership in a joint family business is the result of status and not of contract.

(2) The death of a member of joint family, i.e., a coparcener, or even of the managing member does not dissolve the business, and the property in the business passes by survivorship to the surviving members like any other form of joint family property. But a partnership is dissolved by the death of any one partner.

unless there is a contract to the contrary contained in the articles for the continuance of the business by the survivors.

(3) A minor member of joint family business become a member from the moment of his birth by virtue of his status. But in a partnership a minor cannot become a partner. He can be admitted only to the benefits of the partnership by agreement between the partners.

(4) A partner is entitled to ask for an account of past profits when he severs his connection from the partnership. But a coparcener cannot ask for an account of past profits when he severs his connection from the family business or when he takes a portion of the family business<sup>1</sup>.

(5) The rights and liabilities of the coparceners inter se and also in respect of the joint family trade or business are governed by Hindu Law. But the rights and liabilities of partners in respect of the Partnership are covered by mutual contract subject to the Indian Partnership Act.

#### **Relations of partners to one another :**

As partnership is the relation of contract between the partners, the relations of partners to one another may be wholly governed by the terms of the partnership agreement. Thus A, B and C agreeing to form a partnership may agree that A will sign cheques and bills, B will have the right to expel any partner he thinks fit, and C will look after the purchase and sale of the business and so on. But whatever may be the terms of the agreement, or in the absence of any written agreement at all, the following conditions are imposed by law on every such contract:

(1) Utmost good faith. Each partner must observe the utmost fairness and good faith to his fellow partners. That is, partners are bound to carry on the business of the firm to the greatest common advantage, to be just and faithful to one another, and to render true accounts and full information of all things affecting the firm to any partner or his legal representative. Thus, even where a partnership agreement provides that a partner may be expelled for breach of certain specified articles, the other partners cannot actually expel a partner according to this clause.

<sup>1</sup> Ramaswamy Chetty vs. Srinivasa Aiyar, 70 M.L.J. 214, 216

<sup>2</sup> Section 9

except in good faith. It has been held that such a clause will not justify the expulsion of a partner where the motive for the expulsion is really to purchase the interest of the expelled partner on unfavourable terms.<sup>1</sup>

(2) **Duty to indemnify for loss caused by fraud.** Each partner must indemnify the firm for any loss caused to it by his fraud in the conduct of the business of the firm. A, B and C are partners in a business of stockbrokers. A buys certain shares from his brother at a ridiculously high price. The shares go down in price and the firm suffers loss. A must indemnify the firm for the loss.

Apart from the above two provisions the partners may regulate their relations in any way they like by contract. Agreement between themselves. But where there is no contract where one exists but it does not cover all the aspects of the relation between them, the following rules is enacted by the Partnership Act will be deemed to apply and will be relevant to the same.

(1) *The conduct of the firm*

Subject to contract between the partners

(a) Every partner is to take part in the conduct or the management of the business.

(b) every partner is bound to attend diligently to his duties in the conduct of the business.

(c) any difference arising as to continuing or not continuing with the business may be decided by a majority of the partners and every partner shall have the right to express his opinion before the matter is decided but such an opinion may be made as to the future of the business without the consent of both partners.<sup>2</sup>

(d) every partner has the right to inspect and copy any of the books of the firm.

(2) *Mutual rights and liabilities*

Subject to contract between the partners

(a) a partner is not entitled to receive remuneration for taking part in the conduct of the business.

<sup>1</sup> Green v. Howell (1910) 1 Ch 499 per Corlett, Hard M R at P 504 36 Digest 502 167<sup>2</sup>

<sup>2</sup> Section 10

<sup>3</sup> Section 12

<sup>4</sup> Section 13.

(b) the partners are entitled to share [redacted] the profits earned, and shall contribute equally to the [redacted] cost incurred by the firm :

' (c) where a partner is entitled to interest on capital subscribed by him, such interest shall be [redacted] in the profits. But in the absence of agreement [redacted] is entitled to receive interest on the capital contributed [redacted].'

(d) a partner making, for purposes of the business, payment or advance beyond the amount of capital he agrees to subscribe, is entitled to interest thereon at the rate of six per cent per annum from the date of the advance. The reason is that such an advance is not in increase of capital but as a loan on which he is entitled to be paid.

(e) the [redacted] is indemnified by a partner in respect of payments made and [redacted] incurred by him

[redacted] in my individual property conduct of the business; and [redacted], such that in my emergency, for the purpose of protecting, the firm from loss, it would be done [redacted] by a person of ordinary prudence, in his own case [redacted] under similar circumstances.

[redacted] a partner shall indemnify the firm for my loss caused by his wilful neglect in the conduct of the business of the firm.

### (3) Personal profit earned by partner

[redacted] subject to contract between the partners

[redacted] If a partner derives any profit for himself from any action of the firm or from the use of the property or business connection of the firm or the firm name, he shall account for that profit and pay it to the firm. So where a partner gets into a private agreement with a customer of the firm, in relation to goods dealt in by the firm, beneficial to himself only, he will have to share the profits with his co-partners; for he is abusing his position for his own selfishness and to the detriment of the joint business.<sup>1</sup>

<sup>1</sup> Lord Landley on Partnership, 10th Ed. 465

- A Partner is an agent for the firm and this clause repeats the right of an agent as against the principal. See ante "Law of Contract" under the heading *Agency*. See also *Burdon vs. Baskus*—36 Digest 349, 268.

<sup>2</sup> Section 16

<sup>4</sup> Underhill on Partnership—P. 87. See also *Rumell vs. Astwick* (1826), 1 Sim. 52.

(b) If a [REDACTED] carries on any business of the same nature as and competes with that of the firm, he shall account for and pay to the firm [REDACTED] profits made by him in that business.

(4) *To whom does the firm<sup>1</sup> belong?*

(a) Subject to contract between the partners, the property of the firm includes property and rights and interests in property originally brought into the stock of the firm or acquired by purchase or otherwise for the firm, or for the purposes and in course of the business of the firm, and includes also the goodwill of the business.

Unless a contrary intention appears, property and rights and interests in property acquired with the view to belonging to the firm are deemed to have been acquired for the firm.

(f) Subject to contract between the partners, property of the firm shall be held and used by the partners exclusively for the purposes of the business.

#### **Relations of partners to third parties :**

A partner is the agent of the firm for the purpose of the business of the firm. That is why it is sometimes said that the law of partnership is a species of the law of agency. The partners are collectively liable for the acts or defaults of each of them in that each partner is *prima facie* the agent of the firm and of each of his co-partners for the purpose of the business of the partnership. This does not mean, however, that a partner can bind the firm or his co-partners for all acts that he may do on his own behalf. A transaction entered into by one partner on behalf of the firm is binding on the firm and makes the partner liable, provided the following conditions are satisfied:

(a) The transaction is related to the normal business of the firm. If A and B carry on business as partners in a wine shop, a contract signed by A in the firm name to supply books would not be binding on the firm or B unless it is made with the express authority of B, for the supplying of books is not connected with the normal business of a wine shop.

(b) The transaction must be an act for carrying on business.

<sup>1</sup> Section 14.

<sup>2</sup> Section 15.

in the usual way. We have seen above that where the act is not in any way related to the partnership business, the act of the partner cannot bind the firm. But the difficulty arises when an act, though clearly related to the business, is illegal by the firm as not falling within the express or implied authority of a single partner. It has been decided by the Privy Council in *Bank of Australasia v. Brellit*<sup>1</sup>, that a partner can pledge or sell or buy goods, construct or pay debts, draw, make, sign or indorse bills of exchange on behalf of the firm for carrying on business in the usual way.

(e) The transaction must have been carried out by the partner in the firm name or as a partner, continuing on that basis or in any other manner expressing or implying an intention to bind the firm.

(f) The transaction must be one which the partner has either express or implied authority to execute. If it is an act forbidden by other partners and if the third person with whom the partner enters into the transaction knows of the restriction the act will not bind the firm.

The liability in contract of the partner is joint and several liability whether the contract is made by one partner or all of them together. The result is that in case of a breach of contract the third party injured can sue any one partner, or all the partners jointly, and upon judgment if damages are recovered from any one partner, he is always entitled to a reasonable contribution from his co-partners.

#### Partner by holding out :

Any one who by words spoken or written, or by conduct represents himself or knowingly permits himself to be represented, to be a partner in a firm, is liable as partner of that firm to anyone who has on the faith of any such representation given credit to the firm, whether the person representing himself or allowing himself to be represented as a partner does or does not know that the representation has reached the person so giving

<sup>1</sup> (1847), 6 Moo 152, at p. 191

<sup>2</sup> Section 22.

<sup>3</sup> Section 25.

credit. This often occurs when a partner retires but nevertheless allows himself to appear as if he still were a partner.<sup>1</sup>

This is the rule of liability which is commonly known as arising out of the principle of "holding out." It rests on the principle of estoppel as laid down by S. 115 of the Indian Evidence Act which is as follows : "When one person has by his declaration, act or omission, intentionally caused or permitted another person to believe a thing to be true, and to act upon such belief, neither he nor his representative shall be allowed, in any suit or proceeding between himself and such person or his representative, to deny the truth of that thing." It was held in *Mallow, March & Co. vs. Court of Wards*, "where a man holds himself out as a partner, or allows others to do it.....he is then properly estopped from denying the character that he has assumed, and upon the faith of which creditors may be presumed to have acted. A man so acting may be rightly held liable as a partner by estoppel."

It should be noted, however, that where after a partner's death the business is continued in the old firm name, the continued use of that name or the deceased partner's name as a part thereof shall not *of itself* make his legal representative or his estate liable for any act of the firm done after his death.<sup>2</sup> The same may, however, become liable if the legal representative becomes guilty of holding out.

What acts amount to "holding out" depends on the facts and circumstances of every case. Such acts may be either positive or passive. The words "knowingly permits himself to be represented"<sup>3</sup> make it quite clear that conduct in order to amount to "holding out" may be passive. A's name is used as a partner by the firm B<sup>1</sup> in its business dealings. A comes to know of it but does not take any step to stop the use of his name or to warn the public about it. A's silence in this case will amount to "holding out."

#### **Restrictions on the powers of partners :**

We have seen above that subject to contract a partner is entitled to act on behalf<sup>2</sup> of the firm in all matters which are to be

<sup>1</sup> Section 28.

<sup>2</sup> (1872) I.R. P.C. at p. 43.

<sup>3</sup> Section 25.

connected with the business and which are usual for the carrying on of such business. But in the absence of any agreement or usage or custom of trade to the contrary the implied authority of a partner does not empower him to

- (a) submit a dispute relating to the business of the firm to arbitration;
- (b) open a bank account in the name of the firm or his own name;
- (c) compromise or compound my claim or action or claim by the firm;
- (d) withdraw a suit or a writ filed on behalf of the firm;
- (e) admit my liability in a suit previously brought against him;
- (f) require money or payment on behalf of the firm;
- (g) transfer or sell property belonging to the firm; and
- (h) enter into a lease on behalf of the firm.

The reason why a minor is not entitled to do the above acts in the absence of agreement or custom is that a dishonest partner may involve the firm and his conduct is liable if he is allowed to act alone.

### **Minor as a partner<sup>1</sup>**

We have seen in earlier part of study that the law of contract that a minor cannot contract. A partnership can be created by contract alone a minor can't be made a partner in a firm. But with the consent of all the partners for the time being, he may be admitted to the benefit of partnership. Such minor has a right to such share of the property and of the profit in the firm as may be agreed upon and he may have access to and inspect and copy any of the account of the firm. But such minor is not entitled to sue the partners for in a count or payment of his share of the property or profits of the firm, except when he severs his connection with the firm. Such minor is not personally liable for the liabilities of the firm but his share in the business is liable for such liabilities.

<sup>1</sup> Section 19

**When a minor can become a partner :**

A minor admitted to the benefits of a partnership may, within six months of his attaining majority, or of his obtaining knowledge that he had been admitted to the benefits of partnership, whichever date is later, give public notice that he has elected to become or that he has elected not to become a partner in the firm. If he elects to become a partner he will become a partner and if he elects not to become a partner he will cease to be a partner but if he fails to give such notice, he will become a partner in the firm on the expiry of the said six months. When a minor becomes a partner in the above way.

(a) his rights and liabilities as a minor continue upto the date on which he becomes a partner, but he becomes personally liable to third parties for all acts of the firm done since he was admitted to the benefits of partnership, and

(b) His share in the property and profits of the firm after he becomes a partner shall be the share which was given to him by the consent of all the other partners at the time of his admission into the partnership business.

**When a minor elects not to become a partner**

(a) his rights and liabilities shall continue to be those of a minor upto the date on which he gives public notice

(b) his share shall not be liable for my acts of the firm done after the date of the notice, and

(c) he shall be entitled to sue the partners for his share of profits when he severes his connection with the firm<sup>1</sup>

**Registration :**

Registration does not create a partnership. It is the contract between partners which creates a partnership. Registration is only a concrete and reliable evidence of the existence of a partnership. When a firm is registered, the partners cannot deny the partnership to avoid liability. Thus, it affords protection to persons dealing with the firm. But the Partnership Act does not make registration compulsory. It simply provides that an unregistered firm shall suffer from certain disadvantages which may be mentioned as follows:

<sup>1</sup> Section 30.

(1) An unregistered firm cannot sue any third party to Disadvantages of enforce any claim arising out of contract and non-registration exceeding the sum of Rs. 100/-, S. 69.

(2) A partner of an unregistered firm cannot sue his co-partners to enforce his rights as a partner excepting when he sues for the dissolution of the firm or for accounts..

These disadvantages do not, however, attach to a firm whose place of business is outside British India.

### **Formalities of Registration :**

A firm must apply to the Registrar of firms for registration. Each province appoints its own Registrar. The application for registration should be accompanied by the prescribed fee of Rs. 3/-<sup>1</sup>, and it should contain a statement of the following particulars :

- (a) the firm name,
- (b) the place or principal place of business of the firm,
- (c) the names of any other places where the firm carries on business,
- (d) the date when each partner joined the firm,
- (e) the name in full and permanent addresses of the partners, and
- (f) the duration of the firm.

The statement must be signed by all the partners or by their agents specially authorised in this behalf. A firm name must not contain words like Crown, Emperor, Imperial, Royal and so on.

When the Registrar is satisfied that the above provisions have been complied with he shall record an entry of the statement in a register, called the Register of Firms and shall file the statement, and this will amount to registration of the firm. When the name of the firm is changed, or the place of business is changed or any one branch is closed or opened or any new partner is introduced or any old partner retires, all such changes must be notified to the Registrar in a prescribed form and the Registrar will then note the changes in the Register of Firms.

<sup>1</sup> Section 58.

### Dissolution of partnership:

Unless a partnership is dissolved in the meantime a partnership will continue for whatever period of time is specified in the agreement, or where the partnership is for carrying out a particular venture, until the completion of that venture. Where no time is specified it all the partnership is said to be a *partnership at will*. In the case of a partnership at will, any partner can dissolve the partnership by giving notice to all the other partners. This notice may be either oral or in writing.

### **Reconstitution of a firm :**

A partnership firm is said to be reconstituted when any one of the following changes occurs:

(1) Introduction of a new member. A new partner can only be introduced if the contract of partnership provides for it. Otherwise all the partners must agree to the introduction of the new member. Thus, if a partner sells his share in a partnership the purchaser of his share does not become a partner unless all the other partners agree.

A new partner does not in the absence of special agreement, become liable for the debts of a firm existing before he became a partner. He is liable only for those debts which have been incurred after he became a partner.<sup>1</sup>

(2) Retirement of a partner. A partner may retire (a) if the contract of partnership allows him to, or (b) if all the other partners consent or (c) where it is partnership at will if he gives notice of his retirement in writing to his co-partners.

(a) A retiring partner does not in the absence of agreement cease to be liable for the debts of a firm incurred while he was a partner.

(b) A retiring partner may still be liable as an apparent member of the firm in respect of all debts incurred, to old customers of the firm, even after his retirement, unless such old customers have had actual notice of his retirement.

(c) As regards new customers doing business for the first time with the firm after the retirement of the retiring member,

<sup>1</sup> Section 31

<sup>2</sup> Section 32

he retiring member is liable to give a loss, public notice of his retirement.

(d) All the above three rules may be modified by agreement between partner or between him and the firm.

(e) Expulsion of a partner A firm can only be dissolved under the contract of partnership given power to partners and it is left them however when such power is given, such power must be exercised in accordance with the law.

The liability of an expelled member is limited to a returning partner.

(f) Insolvency of a partner A firm can only be dissolved if one partner is soon as he is adjudged insolvent. If the firm is not dissolved unless all the partners are insolvent but one are adjudged insolvents. As soon as a partner is adjudged insolvent his estate no longer liable for any debts he incurred in the firm. He is not liable for any debts of such insolvent partner. There is no need for either the insolvent partner or the firm to give notice of the insolvency of the partner.

(g) Death of a partner A firm should be dissolved by the surviving partner unless he has failed to provide however when the other has died except his estate he does not make suitable arrangements the firm will be dissolved. But when the surviving partner dies he has to be succeeded by another partner or firm should be dissolved.

### Dissolution of a firm:

Dissolution of firm may be voluntary or involuntary. When firm is dissolved it is called dissolution. After dissolved it is followed as:

(i) When the period fixed by the partners is completed except that the partner may withdraw his fresh to continue the partnership at will.

(ii) On the exclusion of a partner from the firm.

In the case of a firm, by will, by a notice from any partner asking for dissolution.

- (iv) By the insolvency of all, or all but one partners.
- (v) By the death of any one partner.
- (vi) By the partnership becoming illegal, e.g., on the outbreak of war.
- (vii) The court may dissolve partnership in the following cases<sup>1</sup>.
  - (a) If any partner becomes a lunatic or permanently of unsound mind, not only the other partners but also the representatives of the lunatic may bring a suit for dissolution.
  - (b) If a partner becomes permanently incapable of carrying out his part of the partnership contract, e.g., physical incapacity or exile, the court, at the instance of any other partner, may dissolve the partnership.
  - (c) If a partner wilfully and persistently commits breach of the partnership contract, the court may, at the instance of any one partner, dissolve the partnership.
  - (d) If a partner becomes guilty of such misconduct as would prejudicially affect the business of the firm, the court may allow a dissolution. The misconduct need not be in course of the business of the firm. It may be connected with matters outside the course of the firm's business. Thus, in Carmichael *vs.* Evans<sup>2</sup>, dissolution was granted by the court on one of the partners being convicted of fraud for travelling in a railway carriage without a ticket.
  - (e) At the instance of the other partners, if any partner transfers his interest in the firm to a third party, or allows his interest in the partnership to be charged for his own separate debts.

<sup>1</sup> Section 44.  
<sup>2</sup> 19(1914) 1 Ch. 486

- (f) If the business cannot be carried on except at a loss, the court may grant a dissolution
- (g) If in the opinion of the court it is just and equitable to dissolve the partnership, the court may grant a dissolution

### **Effect of Dissolution :**

The rights and obligations of partners on dissolution are as follows :—

1. Notwithstanding the dissolution of a firm, the partners continue to be liable as such to third parties for any act done by any of them which would have been an act of the firm if done before the dissolution, until public notice is given of the dissolution.

Provided that the estate of a partner who dies, or who is adjudicated an insolvent, or of a partner who, not having been known to the person dealing with the firm to be a partner, retires from the firm, is not liable for acts done after the date on which he ceases to be partner.

Public notice may be given by any partner<sup>1</sup>

In Pollock & Mulla's Indian Partnership Act illustrations are given by summarising English cases on this point and it will be worth while reproducing those illustrations here.

(a) A and B, partners in trade, agree to dissolve the partnership and execute a deed for that purpose, declaring the partnership dissolved as from 1st January ; but they do not discontinue the business of the firm or give notice of the dissolution. On 1st February, A endorses a bill, in the partnership name, to C, who is not aware of the dissolution. The firm is liable on the bill<sup>2</sup>.

(b) A bill is drawn on a firm in its usual name of the M. Company, and accepted by an authorised agent. A was formerly a partner in the firm, but not to the knowledge of B, the holder of the bill, and ceased to be so before the date of the bill. B can sue A upon the bill.<sup>3</sup>

(c) A is a partner with other persons in a firm. A dies, and

<sup>1</sup> Section 45

<sup>2</sup> Ex parte Robinson (1833) I. D. & Ch. at p. 388.

<sup>3</sup> Canter vs Whalby (1830) I. B. & Ad. 11.

the survivors continue the business under the same firm. Afterwards the firm becomes insolvent. A's estate is liable to customers of the bank for balances due to them at A's death, so far as they still remain due, and for other partnership liabilities incurred before A's death; but not for any debts contracted or liabilities incurred by the firm after A's death.<sup>1</sup>

2. On the dissolution of a firm every partner or his representative is entitled, as against all other partners or their representatives to have the property of the firm applied in payment of the debts and liabilities of the firm, and to have the surplus distributed among the partners or their representatives according to their rights.<sup>2</sup>

This involves amongst others the right to account and to have a receiver appointed of the assets of the firm for the purpose of preserving the assets of the firm until accounting is completed and the assets distributed.

3. After the dissolution of a firm the authority of each partner to bind the firm, and the other mutual rights and obligations of the partners, continue notwithstanding the dissolution, so far as may be necessary to wind up the affairs of the firm and to complete transactions begun but unfinished at the time of the dissolution, but not otherwise:

Provided that the firm is in no case bound by the acts of a partner who has been adjudicated insolvent, but this proviso does not relieve the liability of any person who has after the adjudication represented himself or knowingly permitted himself to be represented as a partner of the insolvent.<sup>3</sup>

4. If a partner dies and the firm is dissolved any profit, secret or otherwise secured by the surviving partner or the representative of the deceased partner in course of winding up must be thrown into the common fund and held.<sup>4</sup>

5. Where a partner has paid a premium on entering into partnership for a fixed term and the partnership is dissolved before the term, he is entitled to recover his premium unless the dissolution is due to death of one of the partners or to his own mis-

<sup>1</sup> *Dixvane v. Nohl* (1916) 1 Mer 529.

<sup>2</sup> *Brice's case* (1816) 1 Mer 622.

<sup>3</sup> Section 46.

<sup>4</sup> Section 47.

<sup>4</sup> Section 50.

conduct or is in pursuance of an agreement containing no provision for the return of premium paid<sup>1</sup>

### **Application of the assets of a firm on dissolution :**

In settling accounts of a firm after dissolution, the following rules shall, subject to agreement of the partners, be observed<sup>2</sup>

(a) Losses, including deficiency of capital, shall be paid first out of profit, next out of capital and, lastly, if necessary by the partners in dividends in the proportions in which they were entitled to share profits.

(b) The loss of the firm, including sums contributed by the partners to make up deficiency of capital, shall be applied in the following manner and order:

(i) in paying the loss of the firm to third parties,

(ii) in paying to each partner separately what is due to him from the firm for advances, distinguished from capital

(iii) in paying to each partner separately what is due to him on account of capital and

(iv) the residue, if any, shall be divided among the partners in the proportions in which they were entitled to share profits.

Where there are joint debts due from the firm, and also separate debts due from my partner, the property of the firm shall be applied in the first instance in payment of the debts of the firm and if there is any surplus, then the share of each partner shall be applied in payment of his separate debts or paid to him. The share of property of my partner shall be applied last in the payment of his private debt, and the surplus of my share of the property of the firm to the firm.<sup>3</sup>

<sup>1</sup> Section 51

<sup>2</sup> Section 48

<sup>3</sup> Section 49

## CHAPTER IV

### COMPANY LAW

*Indian Companies Act.*

In point of time partnerships preceded Companies. The earliest forms of associations of persons for the purpose of doing business for profit were partnership firms. But with the Industrial Revolution when business became more complicated and far flung and liabilities attaching to business concerns went up by leaps and bounds, it was found that it was not possible to build huge business concerns with a few persons having unlimited liability. To build up a Company like the Tatas would require so many millions of rupees as capital and involve so huge a liability that a partnership of a few persons could not possibly undertake so vast a venture and so big a liability. That is why Companies, with many people subscribing capital and sharing risks and liabilities in a limited way, became a necessity in the modern business world. When many people associate themselves in a Company two things stand out.

(1) The Company becomes a separate legal entity. Unlike a Partnership it becomes a person in the eye of law, separate in existence from the people who are its share-holders.

(2) Unlike a Partnership the people constituting a Company do not become responsible for all the liabilities of the Company unless they agree to be so responsible. They are liable, usually, only up to the amount of their shares or any other amount which they fix up by mutual agreement.

A Company can, therefore, be defined as a separate legal person brought into existence by registration or incorporation under the Indian Companies Act of 1913 as amended by Act XXII of 1936 and Act II of 1938, in pursuance of several people agreeing to form themselves into a Company. A Company is also known as a corporation.

#### Kinds of Companies :

There are two types of Companies—Private and Public. The main points of difference between the two classes of Companies may be described as follows :—

(1) A Private Company cannot have more than 50 members. But a Public Company can have any number of members.

(2) A Private Company must have in its articles restrictions on the rights of transfer of shares. But a Public Company need not have such restrictions.

(3) A Private Company cannot invite the public to subscribe for any shares or debentures in the Company. But a Public Company suffers from no such restrictions.

(4) A Private Company can be formed by two persons whereas a Public Company cannot be formed except by at least seven persons.

(5) A Private Company is not bound to issue a prospectus or a statement in lieu of prospectus, whereas in the case of a Public Company a prospectus or a statement in lieu of a prospectus must be issued.<sup>1</sup>

(6) A Private Company is not required by the Indian Companies Act to file its balance sheet with the Registrar. It is also not required to hold the statutory meeting and to deliver the statutory report to the Registrar. But a Public Company must do all these things.

(7) A Private Company can commence its business as soon as it is registered or incorporated. But a Public Company cannot commence its business without obtaining a certificate of commencement from the Registrar. The Registrar will grant a certificate of commencement only when the following formalities are complied with.

(a) When shares amounting to the minimum subscription have been allotted.

(b) When every director has paid for the shares he has taken.

(c) When a statutory declaration has been filed with the Registrar that the above conditions have been complied with.

Apart from all the provisions mentioned above or any other express provision contained in the Companies Act, a Private Company must conform to all the provisions enacted in the Com-

<sup>1</sup> For prospectus or a statement in lieu of prospectus see part.

panies Act. Thus, Lord McNaghten said in *Trevor vs. Withworth*:<sup>1</sup> "the company was a family company. But if the family company, whatever the expression means, does not limit its trading to the family circle and if it takes the benefit of this Act, it is bound by the Act as much as any other company. It can have no special privilege or immunity."

### **Partnership and Company:**

Partnerships and Companies are both legal entities, i.e., associations in which several people are associated for the purpose of carrying on business for profit. But there exist important differences between these two forms of business organisations which may be enumerated as follows:

(a) A partnership is not a separate legal entity apart from the partners. A firm may mean the partners who constitute it. Therefore, partners can contract only between themselves and can't contract with the firm—such as to take an illustration. A, B and C are three of the firm Martin & Co. Martin & Co. is not a distinct person in the eye of law. A, B and C can make any contract subject to the Partnership Act, and make any arrangement between themselves. But A or B or C cannot make a contract between himself on the one hand and the firm Martin & Co. on the other as Martin & Co. is not a separate person.

But a company is a body not being a separate legal person. It has an independent existence apart from the shareholders who constitute it. Consequently any shareholder can make a contract between himself on the one hand and the company on the other, as the company has a separate existence in relation to him. This point was finally decided in *Solomon v. Salomon*. The facts of the case were as follows. Salomon had a boot business. Later on he formed a company named Salomon & Co. with only seven members, namely himself, his wife, his daughter and his four sons and with a capital of

<sup>1</sup> 12 A.C. 419 at 434

<sup>2</sup> (1897) A.C. 22.

£40,000 To this newly formed company, he sold his old business for £50,000 The company instead of paying Silomon in cash, gave him 20,000 fully paid £1 shares and £10,000 in debentures so Silomon lent the company £10,000 Apart from Silomon's 20,000 shares his wife daughter and sons took only one share each Subsequently the company was wound up The assets of the company were valued at £10,000 out of which to pay £10,000 due to Silomon and secured £1 debenture and further £7,000 due to unsecured creditors The unsecured creditors claimed that Silomon & Co were really Silomon himself as he held most of the shares The court Silomon could not owe to Silomon himself As such the unsecured creditors should get their £7,000 first but the court held that Silomon & Co was apart from Silomon and therefore Silomon could be sued from the company's assets

Once a company is incorporated it must be treated like any other independent person and the motives of those who founded it are irrelevant<sup>1</sup>

- (b) A partner cannot transfer his share without the consent of his co-partners but in a company there is no restriction as regards the transfer of shares
- (c) Each partner is an implied agent of the partnership for the purposes of the firm business and he can bind the firm and his other partners by his acts related to the normal business of the firm But a shareholder of a company is not an agent of the company A company acts through its directors
- (d) The liability of each partner for the debts of the firm is unlimited so a creditor of the firm can sue any one partner or all the partners jointly for the repayment of his claim But the liability of the shareholders in a company is generally limited unless the shareholders choose to form an unlimited liability company
- (e) Partners may make any agreement between themselves regarding the conduct management or constitution of the partnership But the Companies Act does not allow certain arrangements to be made between the share-

<sup>1</sup> Topham's Company Law 9th ed., p 6

holders of a company, e.g. a company cannot buy the shares of the members

- (f) In a partnership, in the absence of any agreement, each partner is entitled to take part in the management. But in a company, the management is generally carried on by the directors only and a shareholder has not any right to take part in the management of the company simply because of his membership.
- (g) The object of a company can only be altered by a special procedure subject to confirmation by the court. But the object of a partnership can be changed by agreement between all the partners.

### **Formation of Companies :**

#### *Steps in the formation of a Company*

In studying Company Law we should be clear about the different stages which are necessary for the formation of a company. In the *first stage* a few people known as promoters get together to form a company. The function of a promoter is that of one who undertakes to form a company with reference to a given object and to set it going and who further the necessary steps to accomplish that purpose.<sup>1</sup>

In the *second stage* the promoter or promoters, when they decide on forming a company, must fix up five things—(a) *Object or purpose* for which the company is to function (b) The name of the company (c) The place where the business of the company is to be carried on (d) How far each member undertakes to be responsible for the liabilities of the company (e) The amount of capital necessary for successfully carrying on the business of the company. The promoters incorporate their decision "on these five points in a document called the *Memorandum of Association*. In the *third stage* the promoters have to decide *how* the business of the company is to be carried on. Arrangements have to be made for the appointment of directors who will conduct the business of the company, the division and allotment of shares, meetings of shareholders and all other things necessary for the internal administration of the company. These arrangements are embodied in a document called the *Articles of Association*. In the *fourth stage*

<sup>1</sup> *Twyford v. Grant* (1877) 2 C.P.D. 541.

the promoters have to get the company registered by the Registrar of joint-stock companies after submitting information regarding the Memorandum, the Articles, the names of directors and so on. In the fifth stage a private company can commence business as soon as it is registered. But a public company have then to issue a prospectus inviting the public to subscribe for shares. They can commence business only after a few more formalities have been completed with. We shall now discuss each of these stages in detail.

### Promoters :

In the case of a public company at least seven persons and in the case of a private company at least two persons are necessary to form a company. We have seen before that the few people who form a company for a given object in the very first stage and set it going are known as promoters.

### Memorandum of Association :

This document is the primary constitution, the framework within and inside which the company has to function. It defines the object and limits the power of the company. The shareholders, even if they are unanimous, cannot authorise an act which goes beyond the object or powers granted by the Memorandum.<sup>1</sup> According to the Indian Companies Act, the memorandum must contain the following:

- (a) *The name*—The Company may choose any name, provided the following rules are complied with.
  - (i) The name must be legibly shown on every place of business and every document issued by the company.
  - (ii) The name must not contain, without sanction in writing from the Governor-General in council, words such as Royal, Imperial, Federal, State, etc.
  - (iii) The name must not be identical with, or too closely resemble, the name of any other Company or Firm, nor may such a name be chosen as is calculated to mislead the public into confusing it with that of an existing business. In the first case the Registrar may refuse to register the company, and in the second, the person or

<sup>1</sup> *Ashbury Railway carriage Co. v. Riche* (1875), L.R. 7 H.L.P. 672.

<sup>2</sup> Section 6.

company who is prejudiced may sue for an injunction restraining the Company from using such a name. In *Societe Panhard et Levassor vs Panhard Levassor Motor Co Ltd*<sup>1</sup>, a well-known French Company which was not registered in England but whose cars were sold in England wanted to have itself registered in England. An English Company registered itself with only seven members and with a name which was likely to mislead the public into confusing it with that of the French Company, for the purpose of preventing the French Company to register itself in England. The French Company sued the English Company and the Court restrained the English Company from using the name.

(iv) The word 'limited' must be used as the last word of the name. If any officer of the Company makes a contract on behalf of the company without the word 'limited', he will be held liable on the contract personally, as the Company will not be bound by such contract. Thus in *Atkins & Co Ltd vs Wurdle A, B and C*, the directors of the South Shields Salt Water Baths Co Limited, accepted bills thus - "Accepted A, B and C, directors of S. Shields Salt Water Baths Co". The Court held that A, B and C, were personally liable on the bill as they signed without using the word 'Ltd'.

If a Company, which has been already registered under a name wants to change its name, it can do so by passing a special resolution to that effect and by obtaining the sanction of the local government for the change. The Company must send a copy of the special resolution with the sanction of the local government to the Registrar so that the Registrar can issue a certificate noting the change.

(b) *Registered office*. The memorandum must mention the registered office and the province in which the office is situated so that all communications to the company may be properly addressed.

(c) *Objects*. This clause contains a list of the business and acts which the company has power to transact. Any business may

<sup>1</sup> (1901) 2 Ch. 513.

<sup>2</sup> (1889), 58 L.J.Q.B. 377

be included which is not illegal or against public policy, a restraint of trade and the effect of the enumeration of the object in this clause is that the company cannot do anything outside the powers given in the Memorandum anything so done becomes ultra vires and the Memorandum cannot be changed without leave of the court. If it is so done by the directors which is *ultra vires* it is void. The company cannot make it valid even if every member assent to it. In *Ashbury Railway Company v. Riche* the memorandum of the company gave the power to "and all other things". The company bought a railway crossing which power is not given in the memorandum. It was held that the purchase was valid. If every shareholder had been in the room and every shareholder had said that is a contract which we authorise the board to make it would be valid.<sup>1</sup>

The powers contained in the memorandum should not be interpreted strictly. A company may have powers to do the following acts which are not necessarily contained in the objects clause.

- (l) Power to do any act which is incidental or necessary to the objects of the business. In *Foster v. London Clothier and Dyers Railway Co.* it was held that it was within the implied powers of a Railway Co. to let out inches on which the railway was erected, is being fairly incidental to the objects of the Railway Co. This does not however give a power to do other business which can be conveniently combined with the company's business. Thus it was held in *Attorney General v. London County Council* (1902) AC 165, that the County Council could not run omnibuses to feed the tramways where it Memorandum contained power to run tramways only.
- (m) An act permitted by the Companies Act e.g. to alter its name or its articles to reduce its capital etc.
- (n) Powers to appoint servants and agents to carry out its business.

<sup>1</sup> i.e. beyond the powers of - Topliss's Company Law 9th ed p 1875), LR 7 HLP 672

<sup>1</sup> Per Lord Cairns I C

<sup>2</sup> (1895) 1 QB at p 711

(iv) Power to borrow in the case of trading companies.

(d) A clause stating that the liability of members is limited whether by shares or by guarantee. If the liability is limited by shares, no member can be called upon to pay more than the nominal amount of his share or so much thereof as remains unpaid. Where it is fully paid up the member's liability is nil. If the liability is limited by guarantee, each shareholder undertakes to meet the debts of the company upto a specified sum, e.g. Rs. 50/- or Rs. 100/- and so on, irrespective of the amount of shares he takes.

(e) *Capital clause* This clause states the amount of capital which the company is authorised by its memorandum to raise, the number of shares into which it is divided and the value of each share. The company cannot alter this share capital unless it is authorised by its Articles and allowed by the court to do so. That is why it is known as 'Authorised capital'. It is also known as Registered or Nominal capital. (*N.B.*—Let us anticipate here a few things which comes after the company is registered or incorporated. The whole of the *authorised capital* is not usually offered to the public for subscription. The portion of this capital which is actually offered to the public is known as *Issued capital*. The portion of the issued capital which has been actually taken up by the public and allotted is called the *Subscribed capital*. And the portion of the *subscribed capital* which is actually paid up by those who have taken them is known as the *Paid up capital*. The portion of the *subscribed capital* which remains unpaid is known as the *uncalled capital* which the shareholders can be called upon to pay whenever occasion arises.)

Where capital has been divided into different classes of shares, the rights of the different classes need not be set out in the memorandum. They can be set out in the Articles. But where such rights are set out in the memorandum and no provision is inserted for altering these rights, no alteration can subsequently be made without the consent of the court.

*N.B.*—The classes of shares which the memorandum may contain are the following—

(i) *Preference shares*—The holders of these shares enjoy preference over all other shares in respect of participation in the dividend or the assets of the Company in case of winding up or both. They also have a prior claim to dividend at a fixed rate determined by the

memorandum or articles before any dividend is allowed on any other class of shares.

- (ii) *Ordinary shares*—The holders of this class are entitled to dividend out of net profits after the payment of dividend on the preference share.
- (iii) *Deferred shares*—The holders of such shares are entitled only after other classes of shares have earned certain rates of dividend as per terms defined in the memorandum or the articles.\*

(f) *Association and subscription clauses*: These clauses contain a statement of the desire of persons who signed the memorandum, i.e. the promoters, to be formed into a company and it contains an agreement to take at least one share each. There must be at least seven subscribers in the case of a public company and two in the case of a private company<sup>1</sup>. The agreement to take shares contained in this clause is absolute and binding even though the company never commences its business, and it cannot be set aside on the ground of misrepresentation.

#### **Alterations of the Memorandum<sup>2</sup>:**

(1) *The name*—We have seen before how the name of a company may be changed.

(2) *Registered office*.—We have also seen before how the registered office of a company may be changed.

(3) *The objects*.—The objects of a company can be changed only if the following conditions are complied with:

- (a) The alteration must be passed by a special resolution of the company.
- (b) Notice must be given to every debenture-holder or other persons affected by the change.
- (c) Every creditor who objects must be paid off or his debt must be secured to the satisfaction of the court.
- (d) The alteration must be sanctioned by the court upon a petition duly presented. The court will sanction the alteration only if the alteration is necessary to enable the company—

\* For a detailed study of different classes of shares see *post*.

<sup>1</sup> Section 5.

<sup>2</sup> Sections 11 and 12.

- (i) to carry on its business more economically or more efficiently ; or
  - (ii) to attain its main purpose by new or improved means ; or
  - (iii) to enlarge or change the local area of its operations.
- Thus, in *Re. Indian Mechanical Gold Extracting Co.*<sup>1</sup> a company which had power to work certain patents in India only were allowed by court to work elsewhere and the memorandum was changed accordingly ; or
- (iv) to carry on some other business which may be conveniently combined with its own ; thus, in *Re Patent Tyre Co.* a company manufacturing tyres was allowed to change its memorandum so as to enable it to carry on test and finance business. The new business need not be similar. On the other hand similarity of the new business is not necessarily a ground for sanction, particularly if the new business conflicts with the old. Thus, in *Re Cyclist Touring Club* the club was registered as a Co. with the object of promoting and asserting the use of bicycles and tricycles on the public roads. The Co. proposed to alter its powers by including all tourists including motorists. It was held as one of the objects of the Co. was to protect cyclists against motorists the alteration cannot be allowed.
  - (v) to sell a undertaking, or
  - (vi) to amalgamate with any other company or body of persons.

But no alteration can be made which increases the liability of any member to contribute to share capital or otherwise to pay money to the company.

(4) *Rights of different classes of shares:* If class rights are set out in the memorandum, no alteration can be made in such

<sup>1</sup> (1891) 1 *Sh. 538*

<sup>2</sup> (1907) 1

class rights except on petition to the court or unless such alteration is provided for in the memorandum.

### **Articles of Association :**

These are internal regulations which determine the rights of members is such and regulate the transfer of shares, the conduct of meetings, the appointment of director and other similar matters.

*Differences between Article and Memorandum.*—The article of a company regulates the internal management and working of company. The right of members is to run the company, the relations between members or appointment of directors or the method of voting and such other que<sup>s</sup> as are mentioned in the memorandum are all settled by the articles. But the Memorandum defines the framework within which the article is to function. It determine the relation between the company and the outside world by defining the power of the company is to what thing it can do and what it must do. The article are subject to the memorandum. If they offend any clause in the memorandum they are said to be 'contrary' to that clause. The articles can be altered by special resolution but the memorandum can be altered only under conditions mentioned below.

### **Registration of Articles :**

Under section 17 of the Act no company can be registered by a company if it does not have a registered set of Articles contained in Table A of the First Schedule of the Indian Companies Act which does not apply to them can a regulation contained in Table A to which does not apply as the method of deciding questions of a nature arising from cross transaction business to be arranged by director and so on.

### **Alteration of Articles :**

A company can alter any clause in its articles by a special resolution, provided—

- (a) the altered articles are not illegal, contrary to any statutory provision,

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<sup>1</sup> Ashbury Railway Car Co vs Riche (1875) LR 7 Hl 672

<sup>2</sup> Section 17

<sup>3</sup> Section 20

- (b) the alteration does not seek to increase the liability of the shareholders,
- (c) the alteration does not conflict with the memorandum.
- (d) the alteration is not a fraud on the minority and is made bonafide and in the interest of the company as a whole. Thus in *Brown vs. British Abrasive Wheel Co.*<sup>1</sup>, the majority of the shareholders passed a special resolution altering the articles so as to enable ninetenths of the shareholders to buy out any other shareholder. It was held that the alteration was void as it was a fraud on the minority. But in some cases the majority can even alter the articles so as to be able to exclude the minority where this is done bonafide for the benefit of the company. Thus, in *Sidc bottom vs Kershaw, Leese & Co.*<sup>2</sup>, the articles were altered in such a way that the directors could require any shareholder who was competing with the company to transfer his shares at their full value. It was held that the alteration was valid as it was for the benefit of the company as a whole.

### **Registration :**

The Memorandum and the Articles (if any) must be signed by at least seven persons in the case of a public company and two persons in the case of a private company each of whom must subscribe at least one share of the company. Then they have to be filed with the Registrar of Joint-Stock Companies, along with the following particulars:

- (a) A list of persons who have agreed to act as directors.
- (b) The written consent of those whose names have been given as directors as per above, that they have so agreed.
- (c) A statement as to the address of the Registered Office.
- (d) A contract of directors to take qualifications shares, i.e. the minimum number of shares, which according to the articles a director must take, where they have not subscribed to the memorandum.
- (e) A declaration from an advocate, attorney or pleader that

<sup>1</sup> (1919) 1 Ch 290.

<sup>2</sup> (1920) 1 Ch. 154.

the provisions of the Indian Companies Act have been complied with.

The Registrar after he is satisfied that all the requirements have been complied with and the prescribed fees have been paid, enters the name of the company in the register and issue a certificate of incorporation. The company comes into existence as legal person from the moment the certificate of incorporation is issued.

### **Prospectus :**

A private company can commence its business immediately after it is incorporated. But a public company has to issue a prospectus inviting the public to subscribe to shares in order to raise the minimum subscription without which it cannot commence business. The Indian Companies Act defines a prospectus as any prospectus notice circular advertisement or other invitation offering to the public for subscription or purchase any shares or debentures of a company but shall not include any trade advertisement which shows on the face of it that a formal prospectus has been prepared and filed. In order to be an offer to the public it must be an offer to any person who chooses to come in and take the share. And therefore a private offer to friends does not make the document a prospectus. The prospectus is usually issued immediately after the incorporation of the company. It must be dated and signed by all persons named as director or their authorised agents.

A copy of the prospectus must be filed with the Registrar before it can be issued in order to prevent the public from being misled or defrauded by the optimistic picture generally portrayed by a prospectus. Section 93 of the Indian Companies Act requires that every prospectus must contain the following facts— (1) The contents of the memorandum with names, descriptions and addresses of signatories, and the number of shares subscribed for by them. (2) The number of founders' shares if any, and the nature and extent of the interest of the holders in the property and the profits of the company. (3) The number of redeemable preference shares intended to be issued together with the date and proposed method of redemption. (4) The number of shares (if any) fixed by the articles as the qualification of a director and any provision in the articles as to the remuneration of the

declaration of the secretary or one of the directors in a prescribed form to the effect that shares to an amount not less than the minimum subscription have been allotted and that every director has taken and paid the amount due on application and allotment of his share. On this the Registrar grants a certificate for commencement which entitles the Company to commence business forthwith<sup>1</sup>.

### **Liability for Statements in Prospectus:**

'A contract to take shares is governed by the same rules as other contracts.' Therefore, for untrue statements in the prospectus, liability is on the company in the first instance under the general law of contract.

If a person who subscribes for shares proves

- (i) that there is an untrue statement in the prospectus and
- (ii) that he was induced to take the shares in reliance upon it, then he is entitled to set aside the contract on the ground of *misrepresentation*. If he can prove that the misstatement was deliberately made or made recklessly, he will be entitled not only to avoid the contract but also to damages from the company on the ground of *fraud*<sup>2</sup>.

In order however to obtain rescission of the contract he must bring his action as soon as he learns the untruth of the statement and in any event before the winding up of the company. If after discovering the truth he does some act such as attending a Company meeting or receiving dividend which shows an intention or in the language of his election to keep the shares he cannot subsequently rescind.

Apart from liability under the general law of contract, a special liability attaches to all persons who were directors of the Company when the prospectus was issued, persons who had authorised the use of their names in the prospectus or in having agreed to become directors promoters, and all those who had authorised the issue of the prospectus. Under section 100 of

<sup>1</sup> Section 103.

<sup>2</sup> Topham's Company Law 10th Ed p 49.

<sup>3</sup> See ante 'Law of Contract'.

<sup>4</sup> See ante 'Law of Contract'.

the Companies Act all such persons become liable to pay compensation to any one who subscribes for shares on the faith of a prospectus for damage sustained by reason of any untrue statement in it.

But any of the above persons may escape this special liability if he succeeds in establishing one or the following, as defences:

(1) that he believed the untrue statement to be true from the time of the issue of the prospectus down to the allotment of shares and that he had reasonable grounds for that belief; or

(2) in case of a director that he withdrew his consent to become a director before the prospectus was issued and that in fact it was issued without his knowledge or consent; or

(3) that the prospectus was issued without his knowledge or consent and that as soon as he became aware of the public notice of the fact that he had not consented, or

(4) that although he consented to the issue of the prospectus he withdrew his consent to it before shares were allotted and gave a public notice of the fact and with reason for so doing;

(5) that he made the statement upon the authority of someone whom he had on reasonable grounds for believing to be competent; or

(6) that the statement was a copy of an official document.

### **Capital :**

We have seen before that the total capital of a company is divided in four different senses, namely (1) *Nominal* or *Authorised Capital* (2) *Laid Capital* (3) *Subscribed Capital* and (4) *Paid up Capital*. Sometimes the phrase debenture capital is used to denote the amount borrowed by the company and secured by debentures. But the capital of a company should not mean borrowed capital.

We have seen before that the capital of a Company is generally divided into

(1) Preference shares;

(2) Ordinary shares,

(3) Deferred shares.

It may be provided either in the memorandum or in the articles. But it is more convenient to provide for power to divide capital into different classes with special rights in the articles.

is the articles can be changed by only a special resolution, with the leave of the court. But if the different classes and their rights are fixed by the memorandum, they cannot be altered without the sanction of the court, unless the memorandum itself provides that they may be altered in some particular manner.

Let us now study the different classes of shares.

### (1) Preference Shares :

The holder of these shares is usually entitled to a fixed rate of dividend, say five per cent before any dividend is paid on the ordinary shares. But in such case unless the articles expressly provide, he cannot get more than five per cent however prosperous the company might be.<sup>1</sup>

### Cumulative and Non-cumulative :

Preference shares may be either *cumulative* or *non-cumulative*. In case of cumulative preference shares if the company is not able to pay the fixed dividend in any year owing to profits being insufficient the deficiency is made up out of the profits of the subsequent years. Preferential shares are always deemed to be cumulative unless they are made non-cumulative by express provision or by any language which is sufficiently clear e.g. if the articles provide that preference share shall be entitled *out of the net profits of each year* to a preference dividend of six per cent. In the case of non-cumulative preference shares if dividend is not paid in any one year the deficiency cannot be carried forward as a charge on the profits of the succeeding year.

Preference shares can also be either—(i) *preferential as to capital* or (ii) *Non preferential as to capital*. Where they are made *preferential as to capital* on the dissolution or winding up of the company if any surplus assets of the company is left after meeting all the debts it must be applied first in paying off the holders of these shares. But where they are *non preferential* their holders are paid off equally with the holders of ordinary shares.

### Redeemable Preference Shares :

Generally a company cannot pay back the capital subscribed by shareholders without the sanction of the court. But by

<sup>1</sup> *Staples v. Eastman Photo Co* (1896) 2 Ch 303

Sec. 105 (B) of the Companies Act a company can, in the articles so provide, issue preference shares on condition that they may be redeemed out of a "capital redemption reserve fund," created out of profits for this purpose or out of the proceeds of a fresh issue of shares or out of the sale proceeds of any property of the company.

**(2) Ordinary Shares :**

The holder of these shares is entitled to dividend out of the net profits of the company after the fixed dividend on preference shares has been paid up.

**(3) Deferred Shares or Founders' Shares :**

The holder of these shares is usually entitled to share profits after the dividend on ordinary shares amounts to more than a fixed amount, e.g. the deferred shares may be entitled to half of the profits after a dividend of eight per cent, has been paid on the ordinary shares.

*Reserve Capital*—When shareholders subscribe to shares they are usually required to pay only a portion of the full value of their shares, e.g. A subscribes to twenty Rs. 10/- shares in the India Steel Corporation. He will not have to pay Rs. 200/- straight way. He will probably be required to pay only Rs. 5/- on each share, i.e. Rs. 100/- in all. The portion of the subscribed capital which is not paid up is known as 'uncalled capital.' When a company by a special resolution declares that this uncalled capital shall not be capable of being called up except in the event of and for the purpose of the company being wound up, this uncalled capital becomes the *Reserve Capital* of the company. It cannot be called in except on winding up.

**Stock :**

When shares are fully paid up they may be turned into stock. When the capital of a company is consolidated into stocks, it is no longer divided into equal parts or shares, but it may be divided into any amounts. Thus, it would be possible to hold Rs. 5/8/- of stock where the shares originally were of Rs. 100/- each. The chief points of difference between stocks and shares may be enumerated as follows—

- (a) Shares may be fully or partly paid up. But stocks must be fully paid up.

(b) Shares can be issued and transferred only in terms of complete and indivisible units of the capital, e.g. a capital of Rs 1,000 can be divided only into 1,000 Re 1 shares or 200 Rs 5/- shares or 100 Rs 10/- shares and so on. And a share cannot be bought and sold in fraction. If it is of Rs 5/-, half of it cannot be sold for Rs 2 1/2. But stocks may be issued in lot unlisted in terms of any amount.

(c) Shares are distinctively numbered. But stocks bear no such numbers.

Capital of a company may be altered in the following ways:

- (1) By increasing the Authorised Capital of the company
- (2) By diminishing the Authorised Capital of the company
- (3) By consolidating existing shares
- (4) By subdividing existing shares
- (5) By re-organising existing classes of shares

Let us study each of the above.

#### **Increase of Capital :**

Every company if authorised by its articles subject to such conditions in the article may increase its *nominal or authorized capital* by a resolution of the company in general meeting. If, however, the articles of the company do not authorise such an increase the company may file new articles by special resolution to enable itself to do so. The new capital may be divided into preference ordinary or deferred shares provided it is not contrary to the memorandum. If it is the memorandum may be altered by sanction of the court.

#### **Reduction or Diminution of Capital :**

A company may reduce its share capital by a special resolution, provided it is authorised by the articles subject to confirmation by the court. Reduction is mainly effected in the following three ways:

- (a) Return of paid up capital to the shareholders on the ground that it is not required for the company's purposes
- (b) Reduction or extinction of the liability outstanding on shares on similar grounds
- (c) Writing down of the paid up capital on the ground that

assets have been lost and that the capital is not now fully represented by assets<sup>1</sup>.

If the existing creditors of the company are not affected by reduction of capital, e.g. if it is case (c) above and not case (a) or (b), the court will sanction the reduction and confirm the special resolution. But if the reduction does affect the rights of the creditors, e.g. where reduction is effected as in (i) or (b) above, creditors selected by the court must be given notice of such reduction. If any creditor objects to such reduction, his debt must either be satisfied or secured. When the court is satisfied that all the creditors have either consented to such reduction or their claims have been satisfied or secured, the court will sanction the reduction and confirm the special resolution.

#### **Consolidation :**

Shares may be consolidated by a resolution of the company in the general meeting, e.g. every Re 1/- share may be turned into Rs 10 shares.

#### **Sub-Division :**

Shares may be sub-divided, e.g. every Rs 10 share may be turned into ten Re 1 shares by a resolution of the company in the general meeting.

#### **Re-organisation :**

Capital of a company may be altered by re-organisation, i.e. by altering the rights of the holders of different classes of shares. This can be done in the following ways -

- (a) If the re-organisation is contrary to the memorandum, the re-organisation can be effected by altering the memorandum which can only be done with the sanction of the court.
- (b) If the re-organisation does not require any alteration of the memorandum, i.e. where the rights of the different classes of shareholders are contained in the articles, it can be effected by changing the articles by a special resolution.

<sup>1</sup> Section 55

### **Members and Shareholders :**

The members of a company are those persons who collectively constitute the company. It has been made clear in South London Fish Market Co.<sup>1</sup> that a member is not necessarily a shareholder as an unlimited company or a company limited by guarantee may exist either with or without a share capital. But where the company is limited by shares, the terms member and shareholder are synonymous. Membership in a company is constituted in the following manner :—

(1) The subscribers of a memorandum of a company shall be deemed to have agreed to become members of the company, and on its registration shall be entered as members in its register of members.

(2) Every other person who agrees to become a member of a company and whose name is entered in its register of members shall be a member of the company.

(3) Any person to whom a member transfers his shares and the transfer being recognised by the Directors, his name is put on the register.

(4) The heir or legal representative of a deceased shareholder also becomes a member on his name being substituted on the register.

### **Cessation of Membership :**

Membership is terminated in any of the following manners :—

- (1) Transfer by a shareholder of his share.
- (2) Forfeiture of share for non-payment of calls or otherwise.
- (3) Surrender of share.
- (4) Death of a share-holder.
- (5) By the rectification of the share register and the expunging of the name of a person who has been induced to take shares by fraud and misrepresentation.

### **Transfer of Shares :**

A shareholder has a power to transfer his share under Section 28(1) of the Indian Companies Act, which runs thus : 'The shares and other interests of any member in a company shall

<sup>1</sup> (1889) 39 Ch.D. 324 C.A.

movable property transferable in manner provided by the articles of the Company. Thus a shareholder has a right to dispose of his shares subject only to restrictions imposed by the Articles. The most common form of such restrictions is the requirement of the prior sanction of the Directors for a proposed transfer. Where the articles provide that the sanction of the Board of Directors will be required for effecting a transfer, but they would not be bound to assign any reason for withholding the sanction the transferee title will not be complete without the sanction.

A person who executes transfer form does not cease to be shareholder thereby. He remains liable on his shares until his transferee name is put on the register.

#### **Transfer how effected :**

The transfer must be in writing and the company must not accept a transfer unless a proper instrument in writing has been executed. A transfer need not be by deed unless the articles expressly require it.

A transfer is usually in the following form:

I A B in consideration of the sum of Rs  
 I promise by C D of (hereinafter called the said  
 transfer) do hereby transfer to the said transferee the share  
 shares No. in the undertaking of the  
 company I do I hold in the said transfer the executors  
 administrators and assigns subject to the several conditions on  
 hand I hold the same at the time of the execution thereof and  
 the said transferee do hereby agree to take the said share or  
 shares subject to the condition aforesaid As witness he of  
 or hands the day of

Witness & the signatures etc

The instrument of transfer is executed by the transferor and handed to the transferee with the share certificate. The transferee executes it and sends it to the company for registration. Until registration the transfer is not complete.

#### **Transmission of Shares :**

Transmission of shares differs from transfer in that it signifies passing of shares from one person to another by the operation of law such as by death or insolvency. On the death

of a shareholder his share vests in his personal representatives and his estate remains liable for calls. On the insolvency of a shareholder, the Official Assignee or the Receiver can sell and transfer his shares.

### **Rights of Members :**

A member or a shareholder of a public company has the following rights:

(1) He has a right to transfer his share subject only to the restrictions imposed by the articles.<sup>1</sup>

(2) He has the right to inspect the register of members kept open in the registered office of the company, gratis.

(3) He can require a copy of the register, or of any part thereof, or the list and summary required by the Companies Act or any part thereof, on payment of - 6/- for every hundred words or fraction thereof required to be copied (S. 36).

(4) He can demand inspection of the minute books of general meetings of the company, register of directors, memorandum and managing agent, existent contracts in which any director or directors are directly or indirectly concerned, or interested, and also copies of instruments or charges requiring registration under Section 109 of the Companies Act at all reasonable times (Ss. 43, 97, 91A, 124, 125).

(5) He is entitled to have a copy of the statutory report at least 21 days before the statutory meeting, a copy of the Balance sheet profit and loss account, auditors report and the director's report at least 14 days before the date of the annual general meeting and also of notice of meetings of the company at least 14 days before such meetings (S. 11).

(6) He is entitled to receive a copy of the memorandum and articles within 14 days of his request and on payment of Re 1/- or such less sum as the company may prescribe (S. 25).

(7) He is entitled to be furnished with a copy of the minutes of general meetings within 7 days after he has made a request in that behalf at a charge not exceeding - 6/- for every hundred words (S. 43).

<sup>1</sup> Section 38

<sup>2</sup> Section 36

(5) He can require a copy of the register of holders of debentures or any part thereof, and also copies of mortgages and charges and the company's register of mortgages on payment of -'6/- for every one hundred words required to be copied (S. 124, 125).

(9) He is entitled to be furnished with copies of the Balance Sheets and the Profit & Loss accounts or the income and expenditure account and the auditor's report at a charge not exceeding '6/- for every hundred words (S. 135).

(10) He has a right to apply to the Court for rectification of the share register if (1) the name of any person is fraudulently or without sufficient cause entered in or omitted from the register of members of a company, or (b) unnecessary delay takes place in entering on the register the fact of any person having ceased to be member.

(11) He can apply to the Court to call or direct the calling of general meeting of the company if default is made in holding a meeting in accordance with the provisions of the Companies Act.

(12) He can apply for compulsory winding up of the company on the ground of default in filing the statutory report.

The members in a body are collectively endowed with certain powers. Under the Indian Companies Act they can collectively do any one of the following acts by ordinary resolution and by a simple majority of votes.

1 Increase the share capital by the issue of new shares if the articles authorise the same.

2 Consolidate and divide all or any of its share capital into shares of larger amounts or sub-divide the shares into shares of smaller amounts (S. 50).

3 Convert shares into stock or stock into shares (S. 50).

4 Cancel the shares which have not been taken or agreed to be taken by any person. (S. 50).

5 Discuss and pass any resolution relating to the statutory report in the statutory meeting (S. 77).

6 Appoint the Directors (S. 83 B)

7 Declare dividend, but no dividends declared shall exceed the amount recommended by the directors (R. 95).

8 Consent to the Directors' selling or disposing of the undertaking of the Company or remitting any debt due by a director (S. 86H.).

9 Appoint auditors (S 144)

10 Pass a resolution for winding up of the company when the period, if any, fixed for the duration of the company by the articles expires (S 205)

The members or shareholders can by special resolution do the following

1 Alter the articles (S 20)

2 Alter the memorandum subject to course to the sanction of the court (S 11 & 12)

3 Reorganise the share capital either by reducing increasing the same (S 54 & 55)

4 Appoint inspectors for investigating the affairs of the company (S 142)

5 Wind up the company [S 20(2)]

The members or shareholders can by extraordinary resolution do the following

1 Decide that the company must by reason of its difficulties continue its business and that it is liable to be wound up [S 205(2)]

2 Remove any director whose period of office is liable to determination at any time by removal of directors in rotation before the expiration of his period of office and may appoint another person in his stead (S 6)

### **Duties and Liabilities of Members :**

The duties and liabilities of members are partly contractual and partly statutory. The statutory liabilities are those which the Company is obliged to observe by law. Every shareholder is under a statutory liability to pay in full payment of the money due on shares. Contractual liability is that liability which every shareholder deems he has undertaken. It may and be more important in case of shareholders' rights.

#### **1) Call:**

A shareholder's liability only to the extent of the amount unpaid on his share. Most frequently shares are issued to the public stipulating payment by instalments, e.g. a share of Rs 100 is issued in blocks of Rs 10/- on application, Rs 20/- on allotment, another Rs 20/- in 6 months time and the remaining

Rs 50 who called for. If the company wants the whole or part of the remaining Rs 50/- the director may call. As it already been observed each shareholder's undivided statutory liability to pay the call will portion when called upon. It must be noted that the call must be made strictly according to the manner specified in the articles. Otherwise the call is invalid. It can be usually made by the directors by a resolution at a general meeting and the Secretary give notice of the call to all the shareholders. If a call is made the shareholder need not pay it should be remembereed that a call after the share has not yet voted will not be valid unless it is now required.

The power to make a call is in the hands of the Directors but they have the right to do so for the benefit of the company. If a call is not made the credit of the company he call may be recovered by a member of the company after

Automatic Telephone Co. held that directors could on its own dues but make a call on the other shareholders. It was held that the directors must have some call money off the credit of the non members. It must be made uniformly

### **Forfeiture:**

Forfeiture is a reduction or loss of a member's rights for the violation of the articles. The articles may provide that a member may be forfeited if he does not pay his share of the capital. In the case of Ekinon Motor Industries Ltd. it was held that even if a member does not pay his share of the capital he cannot be removed from the company. It was held that only the court can do so. This is because it is only the court which can decide whether the member has been in default by the directors. It has been pointed out by D. J. J. L. mentioned in the book "Nish Chand & Sons" that the court can do so

<sup>1</sup> Re Gavels & Co. (1889) 4<sup>th</sup> ChD 209

Dawson vs African Cons. Limited Co. (1894) 1 Ch. C. (1900) 2 Ch. 56

<sup>2</sup> G. Newn vs Halle Court So. v. (1915) 2 Ch. 2 (1917) 1 Ch. 146

ture for other reasons may also be valid if it is sanctioned by the articles and if it is exercised bonafide for the interest of the company. It should be noted that the right to forfeit is also a power in the nature of a trust and it will be valid only when it is exercised bonafide for the interest of the company.

### (3) Surrender :

The articles of a company often allow directors to accept surrender of shares. But surrender of shares will most often than not mean the reduction of capital. Partly paid-up shares when surrendered would mean diminution of the share capital to the extent of the unpaid amount of the shares. When these are surrendered it means a diminution of share capital and such surrender is void. But there is no reason to suppose why a surrender of a fully paid up share accepted by the company bonafide and for the interest of the company should not be valid. Of course, if the surrender of the share is nothing but trafficking by the company in its own shares, such surrender is void<sup>1</sup>.

### (4) Lien :

The articles of a company generally provide that the company shall have a first lien on the shares of the members for their debts and liabilities to the company. The result is that the company can claim a charge over the share of a member indebted to the company in preference to the other creditors of the shareholder. But it should be noted that, if the shareholder mortgages his share and the mortgagee gives notice to the company and the shareholder becomes indebted to the company subsequently, the mortgagee will have priority over the lien of the company. But if the shareholder becomes indebted to the company prior to the mortgage, the lien of the company will prevail over the mortgage.

### Dividends :

The dividend means the sum paid and received as the quotient forming the share of the divisible sum payable to the recipient<sup>2</sup>. A company is not bound to divide the whole of its profits amongst the shareholders unless its memorandum or articles clearly provide that it shall do so. Whether the whole or any part shall be

<sup>1</sup> Trevor *vs.* Whitworth (1886), 12 A.C. 418.

<sup>2</sup> Lamplough *vs.* Kent Water Works (1903), 1 Ch. 375.

making a loss, you shall be divided and [REDACTED] investments we [REDACTED] of internal management [REDACTED] company shall [REDACTED] and the Court has no jurisdiction [REDACTED] or restrain it should be noted that the shareholders [REDACTED] [REDACTED] cannot declare a dividend where [REDACTED] have power, the directors to declare a dividend will [REDACTED] at a general meeting and also set aside out of paid up capital a reserve fund before declaring a dividend.

No shareholder, not even a preference shareholder, can sue for enforcing payment until a dividend is declared. The declaration of a dividend creates a debt due from the company to each shareholder and payable at the date at which it is declared. It is made payable. A shareholder can bring a suit if the dividend due to him is not paid by the due date. It has been noted that the dividend must be paid in cash and cannot be paid otherwise such as by the issue of debentures.

### **Rules regarding payment of dividends :**

The most important rules as to payment of dividends are-

1 No dividends shall be paid otherwise than out of profits of the year or any other undistributed properties (R. 97). The decided cases as to the funds out of which dividends will be paid are numerous and, in so far as they attempt to lay down an abstract proposition on this question not altogether easy to understand or to reconcile with one another. In Buckle's "The Law and Practice under the Companies Acts" tenth edition, the position is summarised "as follows:

- (a) That there is nothing in the Act to forbid the distribution of dividend or profits of any description
  - (b) Dividends must not be paid out of capitals, meaning thereby that the company must not under the guise of paying dividend return to the shareholders any part of the money subscribed on the shares. Thus the payment of interests to the shareholders before any profits have been realised out of capital or borrowed money &ultimates
  - (c) That subject to the foregoing clause (b) such questions

<sup>1</sup> Burland & Earne (1902), S.I. 95

<sup>2</sup> Bombay Burma Trading Corp v. Dorabji (1886) 1 Bom. 415

as how the profit and loss account is sanctioned by the whether profits have been earned rest of the core they shall be divided, are primarily held also a power for the directors or shareholders when " accordance with the company's regulations

The profits of a company are the credit balance of profit and loss account properly prepared. They are the sum of receipts over expenses on revenue account. As to what expenses are properly chargeable to capital and what to revenue it is necessarily impossible to lay down any general rule. In many cases it may be for the shareholders to determine this for themselves, provided the determination be honest and within legal limits<sup>1</sup>. In some cases an attempt has been made to express the distinction between what are termed fixed capital and circulating capital, fixed capital being defined as property required and intended for retention and employment with view to it being distinguished from circulating capital meaning property required or purchased with a view to resell it at profit and the remainder being that less the fixed capital need not be movable good but the declaration of dividend but that less a circulating capital must be paid up before any dividend is declared. Let us illustrate what is meant by examples. Suppose that a tramway company lays its line when material and labour are both dear, that both subsequently become cheaper as before and that the same line would be laid for half the money. If at such time the company has sustained a loss in the sense that it is in the altered circumstances the owner of an asset worth only half the sum at which it stands in the Balance sheet. Yet if the company's object is not to traffic in trams but to own them and to make profit by their ownership and working is distributed from the sale, then the loss is a loss on capital account leaving profit and loss account unaffected and it ought for it in the loss account to be divided and divided.

In *Verner vs General Trust* the company was found to purchase investment and to borrow and lend money and the profits is dividend. In 1991 the receipts exceed the expenditure by £22,000 but many of the investments had depreciated

<sup>1</sup> *Tee vs Neuchatel Asphalt Co* 41 Ch D 1

<sup>2</sup> *Verner vs General Trading Trust* (1994) 2 Ch 239

making a loss on the value of the assets of £2,50,000. The investments were intended to be retained and it was held that a company should not be bound to meet every depreciation of its assets by a dividend. For such depreciation may often be only temporary. It was held that the company could declare a dividend under the circumstances. But it was observed that if the business of the company consisted of speculating in investments, the investments would have been circulating capital and may, as such, have been accounted for before any declaration of dividend.

5. A shareholder must wait for the payment of dividends, even when dividends are ample amount, if the directors decline to declare a dividend, except in certain cases.<sup>1</sup>

6. If directors pay dividends out of capital, they may be sued for that in case of the dividends paid. But they may sue a shareholder for dividends received by him if he has not paid over.<sup>2</sup>

7. Profits paid to directors and main profits and may be paid as dividends though there is a loss in capital.

8. As has already been observed the dividends must be paid

### **Interim Dividend :**

The rules of a company usually provide that the directors may pay interim dividends. An interim dividend is a dividend to be paid between two ordinary meetings.<sup>3</sup>

### **Director :**

Every public company must ensure that the directors "are men who are elected by the shareholders from among themselves for the purpose of controlling and managing the business of the company".

### **Directors, Agents of Company :**

What is the position of the directors of a public Company? They are merely agents of the company.<sup>4</sup> The company itself

<sup>1</sup> *Boni vs Burrow Co* (1902), 1 Ch 353

<sup>2</sup> *Re Houl & Co L'd* (1904), 2 Ch at p 213

<sup>3</sup> *Re Jewitt* (1922), 2 Ch 442

<sup>4</sup> Section 83A

cannot act in its own person, for it has no person, it can only act through directors, and the case is, as regards those directors merely the ordinary case of principal and agent for where an agent is liable those directors would be liable. Where the liability would attach to the principal and the man upon whom the liability is the liability of the Company.<sup>1</sup> Thus

(1) If director make a contract on behalf of the company, it is the company the principal who is liable and not the directors they cannot be made personally liable on the contract unless they undertook personal liability either in their own names or by contract on behalf of the company without using the word 'I'd.'

(2) If directors make a contract in their own names but really for the company the other party to the contract can on discovering that the company is the real principal sue the company on the contract.

(3) Where directors enter into a contract which is within the powers of the company to be entered by them in good faith but is beyond the powers of the directors the company becomes the principal in validity the contract.

### **Directors Trustees, in what sense :**

A trust in its simplest form is relation between two persons by virtue of which one of them (the trustee) holds property vested in him for the benefit of the other (the cestui que trust), while as regards the rest of the world he (the trustee) is for most purposes absolute owner of it. The trustee stands in a fiduciary relation with the cestui que trust. He must deal with the property in utmost faith for the benefit of the cestui que trust.

Strictly speaking, the directors of a company are not trustees, because they are not in law when the property of the company may be said to be vested. The property of the company belongs to the company. This is § 10 of the Indian Limitation Act does not recognise director of a company as trustee. But nevertheless, 'the directors i.e. person selected to manage the affairs of the company for the benefit of the shareholders' It is in office of trust which if the undervil it is then duty to perform fully.

<sup>1</sup> See Burns L J in Ferguson vs Wilson 2 Ch App 77

<sup>2</sup> Palmer's Company Law, 16th ed p 164

and entirely<sup>1</sup>." Thus, directors are trustees of the company's funds, money and property and they must deal with these with utmost faith and for the benefit of the share-holders. They will be liable for any dealings with the company's property which is inconsistent with their powers or contrary to the company's rights. But even here there is a difference between directors and trustees. The primary duty of the trustees is to preserve the property. But directors have to carry on business and this involves risk.

Thus Romer J. in the City Equitable case<sup>2</sup> said, "It has sometimes been said that directors are trustees. If this means no more than that directors in the performance of their duties stand in a fiduciary relationship to the company, the statement is true enough. But if the statement is meant to be an indication by way of analogy of what those duties are, it appears to me to be wholly misleading. I can see but little resemblance between the duties of a director and the duties of a trustee."

#### **Appointment of Directors :**

Generally the first directors of a company are appointed by the articles. But if the articles do not provide for such appointment, the subscribers of the memorandum shall be deemed to be the directors of the company until the first directors shall have been appointed. Subsequent directors are appointed by the shareholders in general meeting. Where a director retires or dies before his term of office has expired, the other directors may fill up the vacancy by making an appointment themselves<sup>3</sup>. Usually the method of appointing directors is laid down by the articles and the above rules are subject to the articles. Directors appointed must retire by rotation and at least two thirds of the number of directors must retire at one time.

No person can, however, be appointed as a director by the articles or named or proposed as a director in a prospectus unless before the registration of the articles or the publication of the prospectus he or his agent has—

- (i) signed and filed with the Registrar a consent in writing to act as such director,

<sup>1</sup> Romilly M. R. in York etc. Rail Co. *vs.* Hudson.

<sup>2</sup> (1925), Ch. 407.

<sup>3</sup> Section 83B.

(v) either signed the memorandum for a number of shares not less than his qualification shares, or taken from the company and paid for or agreed to pay for his qualification shares, or signed and filed with the Registrar a contract in writing to take from the company and pay for his qualification shares, or made and filed with the registrar an affidavit to the effect that a number of shares, not less than his qualification, are registered in his name.<sup>1</sup>

**N.B.**—As we have explained before, the articles usually fix a minimum number of shares which every director must subscribe in order to become a director. This minimum number is known as the 'qualification share' and a director must obtain it within two months of his appointment.

#### **Remuneration of Directors :**

Directors cannot claim any remuneration for their work unless the articles provide for it or the shareholders authorise it by resolution in general meeting. The remuneration of directors is a debt owing by company and as such can be paid out of capital.

#### **Vacation of Office by Director :**

A director must vacate his office under S. 84(1) of the Companies Act if—

- (1) he fails to obtain qualification shares within two months of his appointment;
- (2) he is found by court to be of unsound mind;
- (3) he is adjudged an insolvent;
- (4) he fails to pay calls on his shares within six months of such call;
- (5) he or any firm of which he is a partner or any private company of which he is a director, without the sanction of the company in general meeting, accepts any position of profit under the company other than that of a managing director, manager, or a legal or technical adviser, or banker, or accepts loans or enters into contracts with the company;

<sup>1</sup> Section 84(1).

<sup>2</sup> Section 85(1).

(6) he absents himself from three consecutive meetings of the board of directors, or for three months, whichever is longer without leave from the board of directors,

(7) he is convicted of any criminal offence against the company.

### **Powers and Duties of Directors :**

The directors are like trustee in the exercise of the general powers as between the shareholders and themselves and liable accordingly for any dealings with the company ; especially for the exercise of the company's powers which is done with their powers or contrary to the company's rights. They must exercise their powers with good faith and for the interest of the company as a whole. The powers of directors are generally contained in the articles and subject to the articles the directors can do all that is necessary for the proper conduct of the business of the company. The powers of the directors must be exercised by a body by the board of directors unless the articles allow the director to delegate power to some or else or one of them. Generally the articles provide for the giving of special power to one or more directors known as managing directors who actually conduct the business of the company day to day. There are however certain restrictions laid down by the Companies Act on the powers of directors which may be stated as follows:

### **Restrictions on the Powers of Directors :**

(1) The directors of a public company cannot exceed with the consent of the company in general meeting sell or dispose of the undertaking of the company or remit any debt due by a director.<sup>1</sup>

(2) The directors can not make or grant any loan to any of the directors.<sup>2</sup>

(3) A director cannot accept any office of profit under the company except that if he is a director manager technical advisor or banker,<sup>3</sup> fault etc if the company obtained in general meeting appointment ,fault etc

(4) A director pending Act enables to contract for the sale or creation of appointment .

<sup>1</sup> Section 8

<sup>2</sup> Section 9A)

<sup>3</sup> Section 7 B(f)

87 B (b)

purchase or supply of goods and materials with the company without the consent of the other directors.<sup>1</sup>

(5) A director interested in a contract must give notice to other directors about his interest and he cannot attend and vote in the meeting of the board of directors where such contract is to be discussed and considered.

### **Liability of Directors :**

The directors of a company are liable as follows:

(1) They are liable to the company for wrongful application of the company's money, this liability being either in the nature of a breach of trust, by which the director benefits, i.e., accepting a present of qualification share or a gift money, i.e., due to negligence in dealing with the company's property or some money not recognised by the articles or the memorandum or the company papers. Yet, if a company fails to share holders when no profits have been made. But in so far as the directors derive no personal benefit, they are excused if they acted in good faith.

(2) They are personally liable under S. 102 to repay to the shareholders any application made for shares money paid in part or in allotment of shares which was untrue where all or part has taken place before the minimum subscription is to the company. But the directors are excused if they can prove that the fault was not due to any misconduct or negligence on their part.

(3) They are also liable under S. 101 to persons who apply for shares on the faith of misstatements in the prospectus. But there are a number of defences which we have seen before.

(4) They may also become liable on the winding up of the company if it is shown that they were knowingly parties to the carrying on of my business of the company for my fraudulent purpose and, in particular, for the purpose of defrauding creditors.

Directors are, however, exempt from liability under the following conditions

any person

(i) in cases of negligence, managing directors have acted honestly and reasonably, or accept it.

(ii) in cases of errors of judgement.

<sup>1</sup> Section 86 F.

<sup>2</sup> Section 91 B.

(a) in cases of frauds committed by subordinate officers of the company without the knowledge of the director

*N.B.*—But no director can escape liability for his own neglect, default, breach of duty or breach of trust to which he is made liable by ordinary law, irrespective of any agreement or any provision in the article to exonerate him of such liability.

#### Managing Agents:

Managing agent is a person whom a company entrusts the management of the whole affairs of a company by virtue of an agreement with the company and under such control and direction of the director as may be provided for in the agreement.<sup>1</sup> But if the agreement so provides, managing agent may be authorized control and direction of the director. A managing agent may be appointed similarly as far as both are entrusted with the management of the company. If a managing agent is so appointed, but in two or more persons, such managing agents may be collectively called managing agent where such managing agent may be called managing agents and most usually it is found. Such managing agents usually a salaried official subject to the management of the whole business and appointed to manage it for which they are engaged on behalf of the company or the control of the directors.

*Appointment of Managing Agents.*—All power of appointment of managing agent and removal of their office must be granted by the company to the managing agent before the resolution will take effect where such appointment is to be before the issue of the prospectus in which he proposes to name the terms of appointment. A company may always appoint a managing agent by a resolution passed in a general meeting, notice of which has been given to the managing agent. If the managing agent is convicted of a criminal offence relating to the affairs of the company, the managing agent will have to vacate office if he is adjudged in insolvent.<sup>2</sup>

*Duration of Appointment of Managing Agents.*—Before the passing of the Amending Act of 1936 the terms of appointment including the duration of appointment of managing agents were

<sup>1</sup> Section 2 (9A).

<sup>2</sup> Section 87 B(f).

<sup>3</sup> Section 87 B (b).

settled by the agreement made between them and the company. The result was that the promoters could fix any length of time for the appointment of managing agents. But by the Act of 1936 the maximum period for which a managing agent can be appointed is twenty years, after which the managing agent can be reappointed for another term. But a managing agent will continue to function even after twenty years until all claims payable to the managing agent is paid. As regards managing agent appointed before the commencement of the Act of 1936, he can remain in office until twenty years have elapsed from the commencement of the Act, after which he must be reappointed if he is to act as a managing agent.<sup>1</sup>

*Remuneration.* By the Act of 1936 the remuneration of managing agent must be in the form of a fixed percentage of the annual net profit of the company. But a managing agent may insert a provision in the agreement allowing for an allowance a minimum amount in case of absence of or inadequacy of profits. But such a provision can only be effective if the company approves it by a special resolution.

*Restrictions on the Powers of Managing Agents.* There are certain limitations on the powers of managing agents. These are enumerated as follows:

(a) No company can give to a managing agent of the company or to any partner of the firm, or the managing agent in firm or to any director of the private company, if the managing agent is a private company, any loan of the money of the company.

(b) A managing agent if the managing agency consists of an individual or firm or private company, cannot enter into any contract for the sale purchase or supply of goods and material with the company except with the consent of three-fourths of the directors.<sup>2</sup>

(c) A managing agent cannot exercise the power to issue debentures in respect of the company, or except with the authority

<sup>1</sup> Section 87A

<sup>2</sup> Section 87C

<sup>3</sup> Section 87D.

<sup>4</sup> Section 87D(5)

to the directors and within the limits fixed by them, a power to invest funds of the company<sup>1</sup>

(d) A managing agent cannot on his own account engage in business which is of the same nature as and directly competes with the business carried on by the company under his management or by a subsidiary company of such company.

(e) If the articles of a company provide for the appointment of a number of director by the managing agent the number to be appointed by the managing agent must not exceed one third of the whole number of director except in the case of a company<sup>2</sup>.

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## ACCOUNTS AND AUDITORS

### Accounts :

Every company is required by the Indian Companies Act (S. 111) to maintain proper book of account with respect to

- (a) all receipts and expenses and the transactions to which they relate;
- (b) all sales and purchases of goods, and
- (c) the assets and liabilities of the company.

The account books must be kept at the registered office or at other place so may be prescribed by the directors and must be kept open to inspection by the directors during business hours.

### Annual Balance Sheet and Profit and Loss Account :

According to Sec 111 of the Indian Companies Act the Directors of a company must return day not later than 15 months after the incorporation of the Company and subsequently once at least in every calendar year before being held in general meeting a balance sheet and profit and loss account or in the case of a company not trading in profit or income and expenditure account for the period, in the case of the first account since the incorporation of the company and in any other case since the preceding account, made upto a date not earlier than the date of the meeting by more than 9 months or in the case of a company

<sup>1</sup> Section 67G

<sup>2</sup> Section 87H

Section 87I

carrying on business or having interest outside British India for more than 12 months, provided that the Registrar may for any special reason extend the period for submission of such balance sheet and profit and loss account by a period not exceeding 3 months.

A report of the Directors must be attached to the balance sheet as to the state of the company's affairs, the amount recommended to be paid as dividend, and the amounts to be carried to reserve fund.

The balance sheet must contain a summary of—

- (1) the authorised capital
- (2) the issued capital
- (3) the liabilities
- (4) the assets with the particular showing the nature and liabilities of the asset—no showing how the fixed assets have been invested.

The balance sheet must also show—

- 1 the preliminary expenses
- 2 the expenses of my issue or have in debentures,
- 3 the amount of the goodwill, plant and trade mark,
- 4 all the debt of the company which is ascertainable secured on any of its asset must be fitted to be secured
- 5 Commissions and discount on shares and debenture issues
- 6 loans for the purchase of shares by employees,
- 7 the number and amount of my redeemable debenture
- 8 Particulars of debentures which have been redeemed but are available for re-issue
- 9 Shares in and loan to subsidiary companies,
- 10 the balance sheet of a holding company must show particulars as to its subsidiary company
- 11 the amounts and loans to directors and officers,
- 12 the total amount paid to the directors for remuneration.

The balance sheet must be audited and signed by two directors or one if there is only one. The auditor's report must be attached to the balance sheet and read to the company in general meeting.

The profit and loss account must include particulars showing the total of the amount paid whether as fees, percentages or otherwise to the managing agent, if any, and the directors respectively.

as remuneration for their services and the total of the amount written off for depreciation.

The balance sheet and the profit and loss account or an income and expenditure account are to be authenticated in the case of a working company by the manager or managing agent and where there are more than three directors of a company by at least 3 of the directors and where there are not more than 3 directors by all the directors and in the case of other companies by 2 directors or where there are less than two directors by the sole director and by the manager or managing agent (if any) of the company.

A copy of the balance sheet and profit and loss account or an income and expenditure account together with a copy of the auditor's report must be sent to the registrar and every member of the company at least fourteen days before the meeting at which same are to be held before the members of the company.

After the balance sheet and profit and loss account or the income and expenditure account as the case may be have been sent before the company's general meeting, copies thereof and by the manager or secretary of the company must be filed with the Registrar within 31 days after the date of the general meeting. If the balance sheet is not passed at the general meeting statement to that effect and of the reasons therefor must be made to the balance sheet and to the copies thereof required to be filed with the Registrar.

If in any return report, balance sheet, or certificate any statement is made which is for any reason not true as regards any material particular, and if it is done willfully knowing it to be false, the person so doing is punishable with imprisonment and fine.

#### **Auditors :**

It has already been noticed that the annual balance sheet and the profit and loss account of every company must be audited once a year by an auditor. The articles of a company usually provide for the appointment of auditors as follows:

The first auditors may be appointed by the directors before the statutory meeting, and if so appointed they will hold office until the first annual general meeting, unless previously removed by resolution of the members of the company in general meeting, in which case such members at that meeting may appoint auditors.<sup>1</sup>

<sup>1</sup> Section 144 (2).

Subsequently a company must appoint at each annual general meeting an auditor or auditors to hold the office until the next annual general meeting. If it is proposed to appoint a person other than the retiring auditor, notice of intimation to nominate that person to the office of auditors must be given by a member of the company to the company not less than fourteen days before the annual general meeting, and the company must thereupon send a copy of such notice to the retiring auditor and give notice thereof to its members either by advertisement or in any other manner allowed by the articles not less than seven days before the annual general meeting.

The following persons cannot be appointed Auditors —

- (a) A director or officer of the company
- (b) A partner of such director or officer ( except in case of a private company)
- (c) Any person related to the company, but if any person becomes a partner who becomes related to it during his appointment shall thereafter be determined.

If no appointment is made by the company the Central Government on the application of a member has the power of appointing an auditor and fixing his remuneration.

An audit may be made before the next annual general meeting by resolution at the annual meeting.

#### **Powers and Duties of Auditors :**

The auditors' duties are—

(1) To call upon the members of the company on the account of which a balance sheet every financial year, and to receive 14 days before the company in annual meeting, during their tenure of office and the report must state—

- (a) Whether or not they have obtained all the information and explanations they have required
- (b) Whether or not in their opinion the balance sheet and the profit and loss account referred to in the report is drawn up in conformity with the law; and
- (c) Whether or not such balance sheets exhibit a true and correct view of the state of the company's affairs according to the best of their information and the explanations given to them, and is shown by the book of the company and

(d) Whether in their opinion books or account have been kept by the company is required by s. 150 of the Companies Act.

(2) In order to make a report as mentioned above the auditors have right at all times to the books and accounts and vouchers of the company and are entitled to require from the directors and officers of the company such information and explanation as may be necessary for the performance of the duties of the auditors.

The auditors are entitled to receive notice of and attend any annual meeting of the company at which the accounts which have been examined or reported on by them are to be laid before the company and may make any statement or explanation they are wish respect to the accounts.

The Auditors must make themelves acquainted with the articles and the company's rules and under the Companies Act but they are not bound as to the legal responsibilities.

They must be honest and must exercise reasonable care in the discharge of their duties otherwise they may be sued for damages but only if they do not have nothing to do with the wrong which has been committed. They are not bound with the care of a mind of making up their own mind as to whether the company's accounts are correct or not but they may only pass the opinion that it is correct or not in a financial position. The company at the time of the audit is not bound to accept the audit report as it is. However, if the audited company does not accept the audit report, they are still bound to do so. The law requires that they should publish the audit report and if they do not publish it, they should publish it to the shareholders. They should see that the comparison with the books of the company that it was passed down to is to show the correct financial position.

If the auditors fail in their duty to state the correct finances

<sup>1</sup> In Re London & Central Bank (1897) 2 Ch 673

position of the company and it suffers damage, the auditors are liable for such damage.

### **Qualification and Appointment of Directors :**

No person can be appointed or act as an auditor of any company other than a private company unless he holds a certificate from the Central Government entitling him to act as an auditor of the company. The remuneration of an auditor is fixed by the general meeting which amount is paid by the company.

### **Meetings of the Company and Resolutions :**

The general management of a company is carried on by directors who arrive at particular decisions in the meetings of the board of directors. But the shareholders have to meet sometimes to make themselves acquainted with the affairs of the company. The meetings of shareholders are of three kinds : (1) Annual General Meeting, (2) Extra-ordinary general meeting, and (3) Statutory meeting

#### **(1) Annual General Meeting :**

A general meeting of every company shall be held within eighteen months from the date of its incorporation and thereafter once at least in every calendar year and not more than fifteen months after the holding of the last preceding general meeting. If default is made in calling such a meeting every director or manager of the company who is knowingly and willfully a party to the default shall be liable to a fine not exceeding five hundred rupees and the court may on the application of any member of the company, call or direct the calling of a general meeting of the company<sup>1</sup>. The directors of every company must lay before the company in general meeting a balance sheet and profit and loss account, or in the case of a company not trading for profit, an income and expenditure account, for a period covering nine months from the date of the meeting, and in the case of the first meeting after incorporation, for a period covering eighteen months from the date of incorporation. The balance sheet and the profit and loss account or the income and expenditure account must be audited by the company's auditor and the auditor's report must

be attached thereto. Every company other than a private company must send a copy of such balance sheet and profit and loss account or income and expenditure account so audited together with a copy of the auditor's report to the registered address of every member of the company at least fourteen days before the meeting at which it is to be laid before the members of the company and shall deposit a copy at the registered office of the company for the inspection of the members. The directors must also attach to every balance sheet a report about the state of the company's business, the amount, if any, which they recommend should be paid by way of dividend and the amount, if any, which they propose to carry to a Reserve Fund.

### (2) Extraordinary General Meeting :

All meetings other than the annual meetings or those provided for in the articles are known as extraordinary general meeting. These meetings may be called either by the director or the shareholders. Shareholders holding not less than one-tenth of the issued share capital of the company upon which all calls or other sums then due have been paid, may send a requisition, signed by the requisitionists and stating the objects of the requisition, to the directors for calling an extraordinary general meeting of the company. If the directors fail to call a meeting within twenty-one days of the requisition the requisitionists or a majority of them in value, may themselves call the meeting provided they call the meeting within three months of the requisition. Any reasonable expense incurred by the requisitionists by reason of the failure of the directors to convene the meeting duly must be repaid to the requisitionists by the company and the company may deduct it from the fees or remuneration of the directors.<sup>1</sup>

### (3) Statutory Meeting :

Every public limited company must, within a period of not less than one month and not more than six months from the date at which the company is entitled to commence business, hold a general meeting of the members of the company. This meeting is called the "statutory meeting". The directors must, at least

<sup>1</sup> Section 78.

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twentyone days before the day on which the meeting is held, forward a report to every member of the company. This report must be certified by at least two directors or by the chairman of the directors. This report is called the "statutory report" and must contain the following particulars :—

- (a) The total number of shares allotted.
- (b) The total amount of cash received by the company in respect of all the shares allotted.
- (c) An abstract of the receipts of the company and of the payments made thereout up to a date within seven days of the date of the report.
- (d) The names, addresses and descriptions of the directors, auditors, managing agents or managers, if any, and secretary of the company.
- (e) The particulars of any contract the modification of which is to be submitted to the meeting for its approval, together with the particulars of the modification or proposed modification.
- (f) An account of the preliminary expenses of the company.
- (g) Arrears, if any, due on calls from directors, managing agents and managers.
- (h) Particulars of any commission or brokerage paid or to be paid in connection with the issue or sale of shares to any director, managing agent or manager.

The members of the company present at the meeting shall be at liberty to discuss any matter relating to the formation of the company.

If the directors fail to observe the above rules, they are liable to a fine up to Rs 500<sup>1</sup>.

In case no statutory meeting is held within the last date on which such meeting ought to have been held, a shareholder, creditor or the Registrar may apply to the court for the winding up of the company after the expiry of fourteen days from such last date, and the court may order for winding up in such an event<sup>2</sup>.

<sup>1</sup> Section 77

<sup>2</sup> Sections 162 and 166

### **Rules of Procedure as to Meetings and Votes :**

The meetings of a company are usually called by the directors.

But unless articles provide otherwise two or more persons entitled to members holding, not less than one-tenth of paid up share capital can call a meeting.<sup>1</sup>

The court is also competent to convene a meeting either at the instance of a shareholder or on its own initiative where it otherwise impracticable to call a meeting.<sup>2</sup>

Except in the case of a private company, notice of all meetings in writing must be given to every shareholder at least fourteen

days before the holding of such meetings.<sup>3</sup> The notice should be served personally on every shareholder but if the articles allow it may be served

by post. The notice must be sufficient to show the members substantially the object of the meeting, e.g. a notice of resolution to increase the capital should specify the amount of the proposed increase.<sup>4</sup> If any special business is to be transacted the notice must specify its nature. Thus in *Tiessen v. Henderson*,<sup>5</sup> a notice convening an extraordinary general meeting to consider two alternative schemes of reconstruction was held bad because the notice did not disclose that the directors were interested as underwriters in one of the schemes. The only business which can be validly transacted at the meeting is to confirm or reject the proposal of which notice has been given. Alternatives proposed by way of amendment will not be in order, unless covered by the terms of the notice.

Quorum means the fixed minimum number of members of any body which must be present for the proper and valid transaction of any meeting of that body. In the case of a public company the quorum for meetings of shareholders is generally fixed by the articles. But if the articles do not provide for the quorum then in the case of a public company at least five members and in the case of a private company at least

<sup>1</sup> Section 79 (2)

<sup>2</sup> Section 70 (3)

<sup>3</sup> Section 79

<sup>4</sup> *MacConnell v. E. Prill & Co. Ltd.* (1916) 2 Ch 57

<sup>5</sup> (1899), 1 Ch 861

two members, must be present personally to form a quorum<sup>1</sup>.

The articles of a company usually provide as to who shall be the chairman at meetings. But if the articles are silent, each meeting chooses its own chairman, provided there is a quorum before the election of the chairman takes place. The powers of a chairman are as follows,

(1) He maintains order and conducts the meeting properly.

(2) He has the power to decline the result of a vote taken by show of hands and his declaration is conclusive unless proved wrong on its face.

(3) He has the right to adjourn the meeting at his discretion but only if a case for adjournment has arisen.

(4) If the articles provide he may have a casting vote, in addition to his ordinary vote, exercisable only in the case of equality of votes prior to his using the casting vote.

(5) He may decide points of order and at any time take a vote of the majority on the question whether the discussion shall stop.

**Voting** Every member of a company limited by shares has one vote in respect of each share. If the shares are turned into stock then every member will have one vote in respect of each hundred rupees of stock. A member of any company not limited by shares has only one vote irrespective of the number of shares he may hold.

All questions in a meeting are generally decided by a show of hands. But where voting by show of hand is considered unsatisfactory or where it is undesirable, a poll may be demanded. A poll can only be demanded by at least five members, or the chairman or any member or members holding not less than one-tenth of the issued capital which carries voting rights. The chairman then fixes the time and place for taking the poll and on a poll even absent members may vote through proxies.

A 'proxy' is a stamped instrument in writing authorising a person to vote as proxy for a shareholder at a certain meeting.

**Proxy.** The person so authorised must be a shareholder himself. The proxy must be signed by the

<sup>1</sup> Section 79 [2 (b)]

appointer and deposited at the registered office of the Company at least seventy-two hours before the time of the meeting. There can be no power to vote by proxy unless it is expressly provided for by the Articles.

### **Resolution :**

Resolutions of a company are of three kinds :

#### **1. Ordinary Resolutions :**

That is, a resolution passed by a majority of persons at a general meeting. The resolution is passed in the ordinary way and deals with ordinary business, such as, passing of accounts, appointing directors and so on. No notice need be given of such ordinary resolutions unless the articles so require. But notice of all ordinary resolutions to be proposed at the statutory meeting must be given<sup>1</sup>.

#### **2. Extraordinary Resolutions :**

An extraordinary resolution is a resolution passed by a majority of at least three quarters of the members present at a general meeting who are entitled to vote and do vote, such meeting being convened by notice specifying the resolution and stating that it would be proposed as an extraordinary resolution<sup>2</sup>. It is not necessary that all extraordinary business must be conducted by extraordinary resolutions unless the articles so require. It is usually used to wind up a Company voluntarily on the ground that it cannot continue its business by reason of its liabilities and that it is advisable to wind it up. The articles usually provide that directors may be removed by extraordinary resolution.

#### **3. Special Resolution :**

A special resolution is a resolution which must be passed by a three quarters majority of those entitled to vote, and voting at the meeting, of which at least twenty-one days' notice has been given specifying the resolution and stating that it would be proposed as a special resolution<sup>3</sup>. Special resolutions are necessary for the following purposes among others :—

<sup>1</sup> Section 77 (8).

<sup>2</sup> Section 81 (1).

<sup>3</sup> Section 81 (2).

- (a) to alter the articles of the Company ;
- (b) to alter the memorandum with leave of the Court ;
- (c) to change the name of the Company ;
- (d) to reduce the capital with leave of the Court.

Copies of special resolutions must be sent to the Registrar within fifteen days from the date of their adoption.

### **Borrowing Powers :**

A company cannot borrow unless allowed by its memorandum. But in the case of a Trading or Banking Company such a power is implied even though it is not mentioned in the memorandum. A company may borrow money in the following ways :—

- (a) by issuing debentures or debenture stock ;
- (b) by issuing bills of exchange, hundis or promissory notes ;
- (c) by mortgaging movable properties of the company ;
- (d) by mortgaging immovable properties of the company ;
- (e) by depositing the title deeds of the company and creating an equitable mortgage.

The most important of these methods of borrowing is the issue of debentures or debenture stock. So we shall study this in detail.

### **Debentures :**

A debenture is a document by which a company acknowledges its debt to the holder thereof under certain terms and conditions contained in the document. These terms and conditions usually refer to the interest to be paid, the mode of repayment of the principal and the security given for ensuring these payments.

Debentures can be classified as follows on the basis of the terms and conditions of issue.

(a) *Simple or Naked debentures* :—The company by these debentures simply promise to repay the principal amount lent by the holders and also interest at fixed rates thereon. But such promise is not secured by any specific charge or mortgage of the assets of the company or any part thereof. The holders of these debentures, therefore, are unsecured creditors of the company.

(b) *Mortgage debentures* :—By these debentures the company's promise for payment of interest and repayment of the

principal is secured by some charge or mortgage on the total assets, or any part thereof, of the company. If the debentures are secured by such a specific mortgage on any assets of the company that the debenture-holders become the virtual owners of the assets, the debentures are known as *Debentures with a fixed charge* or *Fixed debentures*. If however, the debentures are secured only by such general charge or lien on the assets that the company can deal with the assets in any way they like in the interest of the business, the debentures are known as *Debentures with a floating charge* or *floating Debentures*.

(c) *Redeemable Debentures* :—These debentures are such that the company reserves the right of paying them off and cancelling them on or after a certain date. Usually the redemption payment is made out of a fund specially created known as the Debenture redemption fund, or out of a fresh issue of debentures.

(d) *Irredeemable or Perpetual Debentures* :—These debentures are such that by the terms of their issue the company is never bound to pay them off except in the case of winding up or default in the payment of interest.

#### **Difference between a Shareholder and a Debenture-holder :**

A shareholder is fundamentally different from a debenture-holder. We may note the differences as follows :

- (a) Money raised by the issue of shares constitutes the capital of the company. But money contributed by a debenture-holder is only a loan due by the company.
- (b) A shareholder is a proprietor of the company. But a debenture-holder is only a creditor of the company.
- (c) A shareholder shares profits either at a fixed rate of dividend or at a variable rate.
- (d) Debenture-holder can be paid off. But shareholders cannot be paid off except where the company is wound up, or a reduction of capital is effected by remitting the un-called money on shares.
- (e) In case of winding up, the claims of debenture-holders have priority over those of shareholders.

#### **Debenture Stock :**

The difference between a debt secured by debentures and debenture stock is very much like the difference between shares

and stock. Debenture stocks need not be of any particular denomination but may be subdivisible into any amount. Debenture stock is, therefore, the whole debt of the company merged in one lump. A debenture stockholder can, as such, lend either Rs. 10/- or Rs. 10.8 or 11/- and so on as part of the total debt of the company, but debenture-holders cannot lend otherwise than in terms of fixed denominations, e.g. Rs. 10/- or Rs. 20/- or Rs. 5/- or Rs. 100/- and so on.

### **Remedies of Debenture-holders :**

A debenture-holder who wants to realise his security and recover the money he has lent, has the following remedies :

(1) If the debenture is registered before the winding up of the company, the holder will be deemed a secured creditor and he will have priority over all other creditors. But if the debenture is registered after the winding up has already commenced, he will rank equally with other unsecured creditors.

(2) He may sue on behalf of himself and all other debenture-holders for the recovery of the money lent. In such a case "the court appoints a receiver, and if necessary a manager and declares the debentures to be a charge on the assets of the company and orders a sale of the property."

(3) He may present a petition for the winding up the company.

(4) He may realise his security by foreclosure and sue when the company fails to make payment of the principal and interest as stipulated in the terms of issue. Foreclosure means the process by which the right of the company to redeem the debentures is closed (i.e. barred).

(5) At any time after the principal money secured by the debenture becomes payable, the debenture-holder may in writing appoint any person or persons to be receiver or receivers of the property charged by the debenture. Any receiver so appointed shall have the power—

- (a) to get in and take possession of any of the property charged;
- (b) to carry on the business of the company;
- (c) to sell any of the property charged;
- (d) to make any arrangement or compromise which he shall consider to be in the interests of the debenture-holders;

(e) to apply to the court to appoint a receiver.

### **Receivers :**

A debenture-holder can appoint a receiver, as mentioned in clause (5) above or he can apply to the court to appoint such a receiver, as mentioned in clause (e) above. A court may also appoint a receiver in a debenture-holder's action for the recovery of money lent, as mentioned in clause (2) above in the following cases :

- (a) if the principal money lent has become due ; or
- (b) if the company is wound up ; or
- (c) if the security, i.e. the debenture is likely to be jeopardised even though there has been no default in payment of interest and no winding up, e.g. if the property of the company is attached in execution of a decree obtained by a creditor of the company, or if the company has closed down its business and so on.

Difference between a receiver appointed by the court and a receiver appointed by a debenture-holder :—

(1) A receiver appointed by the court is the agent of the court and as the court cannot be liable on the contracts he makes, he is personally liable on these contracts. He is, however, entitled to be indemnified if he incurs loss or damage on account of such contracts out of the assets of the company in preference to the claims of the debenture-holders.

But a receiver appointed by the debenture-holders, according to the terms of the debenture, is the agent of the debenture-holders. As such the debenture-holders are liable on the contracts of the receiver unless the terms of the debenture provide that such receiver will be the agent of the company and not of debenture-holders.

(2) A receiver appointed by the court performs his duties much more smoothly as interference with his work or duties would amount to a contempt of court. Furthermore, no suit can be commenced against him or in respect of the property in his hands without leave of the court.

But a receiver appointed by a debenture-holder enjoys no such advantage.

### **Registration of Debentures, Mortgages and Charges :**

In a mortgage the interest in a specified *immovable* property is transferred as a security for a debt, but if *immovable* property

*is made security for payment of money (such money may or may not be a debt) to another without any transfer of an interest in the property, it is a charge.* A debenture, as we have seen before, can be secured either by mortgage or a charge.

The following mortgages and charges created by a company should be registered within 21 days of their creation in order to have them treated as secured debts in case of winding up.

- (a) A mortgage or charge for the purpose of securing any issue of debentures.
- (b) A mortgage or charge on uncalled share-capital of the company.
- (c) A mortgage or charge on any immovable property.
- (d) A mortgage or charge on any movable property.
- (e) A floating charge on the undertaking or property of the company.

*Effect of non-registration :* If any of the above mortgages or charges are not registered as aforesaid, they will be void against the liquidator appointed in the event of winding up and also against other creditors. They will rank only as unsecured debts. In certain cases where the court is satisfied that the delay is accidental, the court may extend the time for registration beyond twenty-one days as aforesaid.

#### **Winding up or Liquidation :**

The legal process by which a company is put to an end is known as winding up or liquidation. When it becomes difficult for a company to carry on its business due to financial embarrassments or the business having becomes illegal or for any other reason, the company stops its business by winding up. The purpose is to realise all the assets of the company, pay off the creditors and if any surplus is left after that, to pay off the shareholders. The Companies Act lays down three modes of winding up :

- (1) Compulsory winding up by the court,
- (2) Voluntary winding up without the intervention of the court,
- (3) Voluntary winding up under the supervision of the court.

Let us now proceed to explain the above three modes.

#### **Compulsory winding up by the court<sup>1</sup> :**

<sup>1</sup> Section 162.

**A company may be wound up by the court**

- (i) If the company has by a special resolution resolved that the company be wound up by the court
- (ii) If default is made in filing the statutory report or in holding the statutory meeting
- (iii) if the company does not commence its business within a year from its incorporation or suspends its business for a whole year
- (iv) If the number of shareholders is reduced, in the case of a private company, below two or in the case of any other company below seven
- (v) If the company is unable to pay its debts. A company is deemed unable to pay its debts-
  - (a) if a creditor to whom the company is indebted in a sum exceeding five hundred rupees serves a written notice on the company to pay and the company does not pay within three weeks,
  - (b) if a creditor who has obtained a decree against the company cannot get his decree satisfied
  - (c) if the court is satisfied after taking into account the contingent and prospective liabilities of the company that the company is unable to pay its debts<sup>1</sup>
- (vi) If the court is of opinion that it is just and equitable that the company should be wound up. Under this last heading, the court has jurisdiction to wind up upon any ground not necessarily similar to the foregoing grounds. In particular the following cases have been held to be within this heading
  - (a) Where the substratum of the company has gone i.e. the principal business for which it was formed has become impossible or impracticable
  - (b) If the company was formed for a fraudulent purpose or is being carried on in a fraudulent manner
  - (c) If the affairs of the company cannot be continued because of a complete deadlock

For the purpose of obtaining a compulsory winding up order

<sup>1</sup> Section 163

of the court, proceedings must be started by a petition for winding up to be presented either by the company, or by one or more creditors, or by a contributory, or by court. by the registrar. A 'contributory' means anyone who is liable to contribute to the assets of the company in the event of dissolution. It usually refers to a partly paid-up shareholder. A contributory can present a petition for winding up only when the number of members is reduced, in the case of a private company, below two, or in the case of any other company, below seven, and the shares in respect of which he is a contributory have been held by him for at least six months during the eighteen months before the commencement of winding up. The registrar is not entitled to present a petition for winding up except when it appears from the balance sheet that the financial position of the company is such that the company cannot pay its debts and the permission of the local government has been obtained for submitting such a petition. The petition for winding up must be verified by an affidavit, a copy of which must be served on the company. The day of hearing is appointed by the court and after hearing the parties and considering all the circumstances of the case, the court may either refuse to grant an order for winding up or order the winding up of the company. If the order for winding up is made, the court generally appoints an official liquidator or liquidators in order to conduct the proceedings in winding up of the company and to perform all such functions as are incidental to the winding up.

#### **Effect of winding-up order by the court :**

A winding-up order of the court has the following consequences :—*(a)* The company is deemed to be wound up from the date on which the petition for winding up was presented.<sup>1</sup> *(b)* No suit or other legal proceedings can be proceeded with or commenced against the company without the leave of the court. The object of this provision is to keep the assets of the company intact in order to pay off the creditors equitably in accordance with the provisions of the Companies Act. If suits were allowed against the company the assets would be wasted.<sup>2</sup> *(c)* If any

<sup>1</sup> Section 168.

<sup>2</sup> Section 171.

person has obtained a decree against the company he cannot execute the decree or attach the property of the company without the leave of court. The object of this provision is the same as above<sup>1</sup>. (d) All the property of the company falls into the custody of the court from the date of winding-up order. The official liquidator takes charge of the properties as the agent of the court. The object of this provision is also to prevent wastage of the company's property to the prejudice of the creditors<sup>2</sup>.

### **Voluntary winding-up :**

"The object of a voluntary winding up is that the company and its creditors shall be left to settle their affairs without coming to the court, and to provide them with every facility for applying to the court if necessary"<sup>3</sup>.

*Ways in which a company may be wound up voluntarily<sup>4</sup>:*

A company may be wound up voluntarily when—

(1) the period fixed in the articles for the duration of the company has expired, or an event upon which, according to the articles, the company is to be wound up has happened, and the company has in *general meeting* passed an *ordinary resolution* to wind up ; or

(2) the company has, for any reason whatsoever, passed a *special resolution* to wind up voluntarily ; or

(3) the company by reason of its liabilities has passed an *extraordinary resolution* that it cannot carry on its business and that it is expedient to wind up voluntarily.

### **Effect of voluntary winding-up :**

(1) The voluntary winding-up is deemed to commence from the passing of the resolution which sanctioned it<sup>5</sup>.

(2) After the commencement of the winding up no shares can be transferred without the sanction of the liquidator<sup>6</sup>. Thus, in Taylor's case,<sup>7</sup> it was held that shares transferred with the consent of the liquidator had the effect of making the transferees members of the company.

<sup>1</sup> Section 232.

<sup>2</sup> Section 175.

<sup>3</sup> Topham on Company Law, 10th Ed., P. 259.

<sup>4</sup> Section 203.

<sup>5</sup> Section 204.

<sup>6</sup> Section 205.

<sup>7</sup> (1897) 1 Ch. 298.

(3) Members cannot alter their status after the commencement of winding-up.<sup>1</sup> Thus, in Castello's Case,<sup>2</sup> it was held that where shares were transferred to a minor after the winding-up the minor could not ratify the transfer after he attained majority as he cannot change his status as a minor after the winding up.

(4) The legal entity of the company and powers appurtenant to that continue to exist until the company is completely dissolved.

### **Kinds of voluntary winding-up :**

There are two kinds of voluntary winding up :

- (A) Member's voluntary winding up.
- (B) Creditor's voluntary winding up.

### **(A) Member's voluntary winding-up :**

To bring about a member's voluntary winding up the following conditions must be satisfied.

(i) The majority of the directors must deliver to the Registrar a statutory declaration that the company is *solvent* and that the company will be able to pay its debts in full within three years from the commencement of the winding up.<sup>3</sup>

(ii) After the above statutory declaration the shareholders must meet and pass a resolution, ordinary, special or extraordinary as the case may be, for the winding up of the company.

The company in general meeting appoints a liquidator or liquidators and fixes his remuneration for the purpose of winding up and distributing the assets of the company among the creditors. On the appointment of a liquidator all the powers of the directors come to an end except so far as the company in general meeting, or the liquidator, sanction their continuance.<sup>4</sup>

If the winding up continues for more than a year the liquidator must summon a general meeting of the company at the end of the first year from the commencement of the winding up

<sup>1</sup> Section 227.

<sup>2</sup> (1869), L.R. 8 Eq. 504.

<sup>3</sup> Section 207.

<sup>4</sup> Section 208 A.

and of each successive year and lay before the meeting an account of his conduct<sup>1</sup>. After the affairs of the company are fully wound up, the liquidator must prepare a final account and call a general meeting of the company called the final meeting which must be properly advertised. Within a week of the final meeting, the liquidator must send a copy of the account and a return of the meeting to the Registrar. The Registrar registers the accounts and returns and at the end of three months from such registration the company is dissolved.<sup>2</sup>

#### (B) Creditor's voluntary winding-up :

Where no declaration is to solvency of the company is made and the shareholders pass a resolution for winding up the winding up is known as creditor's voluntary winding up<sup>3</sup>. The procedure for a creditor's voluntary winding up is as follows<sup>4</sup>:

- (i) The company in a general meeting passes a resolution for voluntary winding up without any prior declaration of solvency by the directors.
- (ii) The company must call a meeting of the creditors for the same day or on the next following day on which the above meeting is held.
- (iii) The directors must lay before the meeting of the creditors statement of the position of the company and a list of creditors.
- (iv) One of the creditors is appointed as the meeting of the director.

The creditors and the shareholders may in their respective meetings nominate a person as liquidator but if they choose different persons to act as liquidator the nominee of the creditors shall become the liquidator.

The credit is any appoint committee of protection consisting of ten members of whom not more than five are to be nominated by the shareholders.

If the winding up continues for more than a year the liquidator must summon a general meeting of the company and a

<sup>1</sup> Section 208 D

<sup>2</sup> Section 208 F

<sup>3</sup> Section 207

<sup>4</sup> Section 209 A

meeting of the creditors at the end of the first year from the commencement of the winding up, and of each successive year and lay an account before the meetings.

On the affairs of the company being finally wound up, the liquidator must make up final account and call final meetings of the company and the creditors and lay the account before the meetings. Within a week after the meetings the liquidator must send to the registrar a copy of the account and a return of the meetings. The registrar shall register the account and the return and on the expiry of three months from such registration the company is dissolved<sup>1</sup>.

#### **Winding up subject to supervision of court :**

When a company is being wound up voluntarily the court may at any moment order that the winding up shall take place under the supervision of the court. "The effect is that the liquidator may exercise all his powers without the sanction of the Court in a voluntary winding up, but subject to such restrictions as the court may direct".

The grounds on which an order for supervision is made will be summarised as follows in *Re Prince of Wales slate Quarry Co* (a) Partiality of the liquidator, or (b) non observance of the rules of winding up; or (c) negligence or dilatoriness on the part of the liquidator in realising the assets or (d) the winding up resolution being obtained by fraud.

The court has a discretion both as regards the passing of the supervision order and as regards the nature of restrictions to be imposed on the liquidator in case the order for supervision is passed. Thus in *Re Watson & Sons*,<sup>2</sup> it was held that the court has power to impose such restrictions even as would turn a voluntary liquidation into almost a liquidation by court or it may relax the restrictions where such is desirable. In these respects the court always respects the wishes of the creditors and contributories.<sup>3</sup>

<sup>1</sup> Section 209 H.

<sup>2</sup> Topham on Company Law, 10th ed., p. 268.

<sup>3</sup> (1868), 18 L.T. 77.

<sup>4</sup> (1891) 2 Ch. 55.

<sup>5</sup> Section 223.

### **Powers of Liquidators :**

Powers of liquidators should be studied under—

- (1) Powers of official liquidator, and
- (2) Powers of liquidator in voluntary winding up.

#### **(1) Powers of Official Liquidator :**

An official liquidator must obtain the sanction of the court in doing anything with respect to the conduct of the winding up of the company excepting that he can take into his custody and control the property and assets of the company and prepare the list of contributors without the sanction of the court. He shall, however, have the following powers with the sanction of the court.<sup>1</sup> :—

- (a) To bring and defend any civil suit or criminal prosecution in the name of or on behalf of the company.
- (b) To carry on the business of the company *so far as may be necessary for the beneficial winding up of the company.* This happens when the liquidator completes contracts undertaken by the company before the winding up and left incomplete at the date of the winding up, which if not completed, would seriously deplete the assets of the company. But this does not mean that the liquidator can undertake new business whose net effect might be to resuscitate the company.<sup>2</sup>
- (c) To sell the property of the company whether by public auction or otherwise.
- (d) To do all acts and to execute, in the name of and on behalf of the company, all deeds, receipts and other documents, and for that purpose to use, when necessary, the company's seal.
- (e) To put forward any claims the company may have on any contributory, i.e. on any holder of partly paid-up share, when such contributory becomes insolvent, so that the company may be paid rateably out of the estate of the insolvent shareholder. For this purpose the liquidator may prove, rank and claim in insolvency.
- (f) To draw, accept, make and indorse any bill of ex-

<sup>1</sup> Section 179.

<sup>2</sup> *Rc Wreck Recovery Co. (1880), 15 Ch. D. 353.*

- change, hundi or promissory note in the name of or on behalf of the company.
- (g) To raise on the security of the assets of the company any money requisite.
  - (h) To do all such other things as may be necessary for winding up the affairs of the company and distributing its assets.

### **(2) Powers of Liquidator in voluntary winding up :**

A liquidator in voluntary winding up may exercise all the above powers without the sanction of the court. In the case of member's voluntary winding up with the sanction of an extraordinary resolution of the company and in the case of a creditor's voluntary winding up with the sanction of the court or the committee of inspection, he can (1) pay any classes of creditors in full, (2) compromise with creditors, and (3) compromise calls, liabilities, debts, and claims between the company and the contributors or other debtors.<sup>1</sup> A liquidator under supervision of the court has the same powers as a liquidator in voluntary winding up subject to such restrictions as the court may impose.

### **Duties of Liquidator :**

The following are the duties of the official liquidator:

- (a) He must keep proper books of account and also minute books in which the minutes of proceedings of meetings must be entered.
- (b) He must submit to the court an account of his receipts and payments at least twice a year.
- (c) He may call general meetings of the creditors or contributors in order to ascertain their wishes.
- (d) He must prepare a list of the contributors after giving them notice and hearing their objection. This list is liable on settled by the Court, the effect of which is to make every person included in the list liable to make contribution towards the assets of company.
- (e) He must collect the assets of the company, make calls as the court directs, and distribute the assets amongst the creditors, and if any surplus be left, to distribute it

<sup>1</sup> Section 234.

<sup>2</sup> Sections 178 A & 182.

amongst the contributories according as the articles provide.

- (f) He must convene a meeting of the creditors within one month from the date of the winding-up order in order to find out whether the creditors want to appoint a committee of inspection to assist the liquidator. If the creditors want a committee of inspection the liquidator must convene a meeting of the contributories to accept the decision of the creditors or reject it. If the shareholders accept the decision, a committee of inspection is appointed with 12 representatives from the creditors and contributories. The committee has the right to inspect the accounts of the official liquidator. If, however, the shareholders reject the decision, the official liquidator must apply to the court for direction as to whether the committee is to be appointed or not, and if appointed as to who should be its members.

The duties of a liquidator in voluntary winding up are as follows :—

(1) In case of a member's voluntary winding up the liquidator must, if the winding up continues for more than a year, summon a general meeting at the end of the first year and of each successive year and lay before the meeting an account of his conduct. The liquidator must also call a final meeting of the shareholders on the affairs of the company being wound up finally.<sup>1</sup>

(2) In case of a creditor's voluntary winding up the duty of the liquidator is the same as (1) above excepting that along with the calling of the general meeting of the company after the first year and also of the final meeting, the meetings of the creditors must also be called.

#### **Distribution of Assets :**

After the assets of the company are fully realised all the expenses in connection with the winding up must be paid first. The surplus is then used to make the following preferential payments.<sup>2</sup>

<sup>1</sup> For details re. final meeting see ante.

<sup>2</sup> Section 230.

- (1) All rates, taxes, revenues and cesses due from the company
- (2) All wages and salary of any clerk or servant, and all wages of any labourer or worker in respect of service rendered within two months before the winding up, not exceeding Rs. 1,000/- for each clerk or servant, and not exceeding Rs. 500/- for each labourer or workman
- (3) Sums due to any employee under the Workmen's Compensation Act, or under any provident fund or pension fund maintained by the company
- (4) The expenses of any investigation by the central government

After the above payments if any balance remains, the unsecured creditors must be satisfied, and if any surplus is left even after that it is to be distributed amongst the contributories, i.e., the shareholders. The above preferential payment do not, however affect secured creditors.

## CHAPTER V

### NEGOTIABLE INSTRUMENTS

The law relating to negotiable instruments in India is contained in the Negotiable Instruments Act of 1881. According to Sec. 13 of the Act a 'negotiable instrument' means a promissory note, bill of exchange or cheque payable either to order or to bearer. It does not mention Hundi which is a very common and important negotiable instrument in India. It does not also explain the nature and characteristics of negotiable instruments. A negotiable instrument may be described as one the property in which is acquired by any one who takes it bona fide and for value, notwithstanding any defect of the title in the person from whom he took it; from which it follows that an instrument cannot be negotiable unless it is such and in such a state that the true owner could transfer that contract or engagement contained therein by simple delivery of the instrument.<sup>1</sup> This definition involves the following characteristics of negotiable instrument, viz.—

- 1 Property in it passes from hand to hand by mere delivery.
- 2 The holder in due course is not affected by defects in title of his transferor or of previous holders.
- 3 The holder in due course can sue in his own name.
- 4 He is not affected by certain defences which might be available against previous holders, e.g. fraud to which he is no party.
- 5 It passes from hand to hand like cash and can be conveniently assigned in discharge of debts.

#### **Promissory Note :**

A promissory note is an instrument in writing (not being bank-note or a currency-note) containing an unconditional undertaking, signed by the maker, to pay a certain sum of money only to or to the order of, a certain person, or to the bearer of the instrument.<sup>2</sup> From this it follows that a promissory note must have the following essential features:

<sup>1</sup> Judge Willis on Negotiable Securities (5th ed.), P 5, 6

<sup>2</sup> Section 4

- (i) It must be in writing. Mere verbal promise to pay is not enough.
- (ii) It must contain an unconditional promise to pay. If the promise to pay is dependent on certain condition which may or may not happen, the instrument is not to be considered as a promissory note. Thus, if A promises in writing to pay B Rs 500/- seven days after his marriage with C or on D's death, provided D leaves him enough to pay his sum the instrument is not a promissory note as the condition of his marriage with C or D's leaving him enough may or may not happen. But if the condition on which the payment depends is one which according to the ordinary expectation of mankind is certain to happen although the time of its happening may be uncertain the promise to pay is to be deemed unconditional (S. 5). Thus if A promises to pay B Rs 500/- on his father's death the promise is unconditional as his father must die in the normal course of things although the time when he will die is uncertain.
- (iii) It must not merely contain an acknowledgment of a debt in writing but must also contain a promise to pay. Thus, if A writes "Mr. B I O U Rs 1000/-" the instrument will not be a promissory note as there is no promise to pay.
- (iv) The amount promised to be paid must be a certain and definite sum of money. Thus, if A promises in writing to pay B Rs 500/- and all other sums which shall become due to him the instrument will not be a promissory note as the amount promised is not a certain and definite sum of money. But the sum payable will be regarded as certain and definite although it may include future interest or is payable at an indicated rate of exchange and although the instrument provides that, on default of payment of an instalment, the balance unpaid shall become due (S. 5).
- (v) It must be signed by the maker. The person who draws the instrument and signs it is known as the maker and the person to whom the promise is made is known as the payee.

(vi) The person to whom the promise is made must also be a definite person. A person may be a definite person although he is mis-named or is designated by description only (S 5)

(vii) Payment must be made in legal money of the country.

We may take the following two examples of promissory note which satisfy all the above conditions

(a) I promise to pay B or order Rs 500/-

(b) I acknowledge myself to be indebted to B in Rs 1000/- to be paid on demand, for value received

The usual form of a promissory note is as follows

Rs. 600/- (Stamp)	Calcutta August 9th, 1941
[Three] months after date [or on demand] I promise to pay A K or order [or bearer] Rs 600/- B G	

Here B G is the maker and A K is the payee

### **Bill of Exchange :**

A bill of exchange is an instrument in writing containing an unconditional order, signed by the maker directing a certain person to pay a certain sum of money only to or to the order of, a certain person or to the bearer of the instrument (S 5) From this it will be seen that the essential elements in a bill of exchange are

(i) A written instrument to which there are three parties, (namely the drawer, the payee and the drawee);

(ii) The instrument must contain an order to pay money, and

(iii) The order to pay must be unconditional

*Difference between a Bill and a Promissory note*

1 In the case of a bill only two parties, namely, the maker or a holder of negotiable instrument and the payee.

exchange to B \_\_\_\_\_ -

mentioned \_\_\_\_\_

payee. 19

2 A promissory note is always presented for payment without any prior acceptance by the maker. But a bill of exchange payable after sight has to be accepted by the drawee or somebody else on behalf of the drawee before it can be presented for payment. In default of such presentation the holder of the bill cannot make any party liable thereon.

A bill of exchange generally arises in the following way. A sends K D goods worth Rs 1000/- In the business world payment is not usually made immediately. A will probably draw a bill and sign it in the usual form as follows -

Rs. 1000/- (Stamp)	Calcutta 9th August, 1941
To Mr. K D Bombay	Two months after date pay P D, or order, the sum of one thousand rupees for value received
	A

A will then present the bill to K D for the latter's acceptance. If K D writes "accepted" across the bill it will mean that K D binds himself to pay Rs 1000/- to P D or order, two months after date. In this case A who draws the bill is known as the *drawer*. K D on whom the bill is drawn is known as the *drawee*. When K D accepts the bill, he is known as the *acceptor*. It may well happen that K D might ask a third person F to accept the bill for him. In this case F will become the *acceptor*. P D to whom the money is to be paid is known as the *payee*. Instead of naming P D, A might have ordered K D to pay him or to his order. In that case A would have himself become the *payee*.

#### **Cheque :**

A cheque is a bill of exchange drawn on a banker and not expressed to be payable otherwise than on presentation. The person who draws the cheque is called the *drawer*, the bank on which it is drawn is called the *drawee*. It must be signed by the maker. It is payable to the *payee* and the person to whom the promise is made is known as the *payee*.

*Difference between cheques and bills*

- (1) A cheque is always drawn on a bank. But a bill can be drawn on any person.
- (2) A cheque need not be accepted by the bank on which it is drawn before it is presented for payment. But a bill payable after sight must be accepted by the drawee before it is presented for payment. In default of such presentation the holder of the bill cannot make any party liable thereon.
- (3) A cheque is payable on demand but in the case of a bill a grace of three days after maturity is allowed in respect of payment.
- (4) In the case of a bill the drawer is discharged from all liability to the payee if it is not presented within a reasonable time. But the drawer of a cheque is discharged from all liability to the payee only if the delay in presentation causes him loss and injury.

**Negotiation :**

When a promissory note, bill of exchange or cheque is transferred to any person, so as to constitute that person the holder thereon, the instrument is said to be negotiated.<sup>1</sup> Where the instrument is payable to bearer it is negotiable by delivery thereof. A, the holder of a negotiable instrument payable to bearer, delivers it to B or B's agent to keep for him. The instrument has been negotiated to B. But where the instrument is payable in order it is negotiable by the holder by indorsement and delivery thereof.

**Indorsement :**

When the maker or holder of a negotiable instrument signs the same, otherwise than as such maker for the purpose of negotiation, on the back or face thereof or on a slip of paper annexed thereto, or so signs for the same purpose a stamped paper intended to be completed as a negotiable instrument, he is said to indorse it of A and is called the indorser.<sup>2</sup> Indorsement is thus a signature made by the maker or a holder of negotiable instrument for the purpose of negotiation.

\_\_\_\_\_  
of B \_\_\_\_\_

<sup>1</sup> § \_\_\_\_\_

<sup>2</sup> § 5101 9

§ &

the *purpose* of negotiation. It is usually the signature of the payee on the back of the instrument. But it might be also the signature of the maker or any holder and might be on the face of the instrument or on a slip of paper attached to it or on a stamped paper where the stamped paper is necessary to complete the instrument.

There are two kinds of indorsement :—

(a) *Indorsement in blank* : An indorsement is said to be 'in blank' if the indorser signs his name only without naming anyone to whom or to whose order the payment is to be made. So long as the indorsement remains in blank the instrument can be transferred by mere delivery as if it were payable to bearer. But even where the indorsement is in blank the transferee cannot get payment unless he signs his own name over the indorsement. (S. 16).

(b) *Indorsement in full* : An indorsement is said to be 'in full' if the indorser not only signs his name but also adds a direction to pay the amount mentioned in the instrument to, or to the order of, a specified person. The person so specified is called the 'indorsee' of the instrument.<sup>1</sup> The indorsee becomes the payee on indorsement and is entitled to sue for the money due on the instrument. The ordinary form of a full indorsement is "pay to A. B. or order" or "pay A. B." A full indorsement prevents the bill from being transferred by anybody but the indorsee ; and none but the special indorsee or his legal representative can sue on it.

#### **Holder :**

The holder of a promissory note, bill of exchange, or cheque means any person entitled in his own name to the possession thereof and to receive or recover the amount due thereon from the parties thereto. Thus, to be a holder a person must be possessed of two rights: (i) he must be entitled to the possession of the instrument by his own right, (ii) he must be entitled to recover the money due on the instrument. Thus, in case of a promissory note payable to A or to his order, A will become the holder as soon as he comes into possession of the note. But if <sup>name</sup> B keeps the note with his agent C for safe custody, B will not be the holder although the instrument is in his possession. The reason is that A has not indorsed the instrument in favour of B and as

such B cannot sue for the money due on the instrument. But if A indorsed the note in favour of B, B would have become the holder.

### **Holder in due course :**

A bill of exchange or a promissory note or a cheque might be either payable to bearer or to order. In the case of a bill of exchange or a promissory note or a cheque, *payable to bearer*, any person who becomes the possessor of such instrument for consideration is known as a *holder in due course* provided he came into possession before the amount mentioned in the instrument became due and he had no sufficient cause to believe that any defect existed in the title of the person from whom he derived his title. A person will not be regarded as a *holder in due course* if he is not in possession of possession without paying value:

mentioned in the instrument, bill of exchange is liable to the drawer defected in his predecessor's title, drawer for the amount mentioned in the instrument had been obtained by him unless it is payable on demand, instrument *payable to order*, must be presented to the drawee person who for consideration has given up his other holder within a reasonable time, before the amount mentioned in the instrument, drawee is not liable to pay unless it having sufficient cause to believe, <sup>acceptance</sup><sup>1</sup>.

Title of the person from whom, exchange is liable to any bona-fide drawer, a bill on B for Rs. 500/- amount mentioned in the bill if the date C is the payee for refuses to pay after acceptance, possession of the instrument by drawer due notice of such refusal becoming the *holder in due course*, refuses to accept or refuses to pay title to the instrument C may the drawee is said to dishonour instrument, indorse it in favour

D the indorsee, will become the <sup>ie</sup> the banker must pay it when possession of the bill before the date for he has got sufficient funds with believe that C had a defective title he banker improperly refuses

**Time for the payment of Negotiable** instrument, compensate the drawer for any loss suffered by the drawer as a result of

A bill of exchange is payable on demand and bound to honour the instrument is mentioned. It is also payable on for instance, limits the specifically mentioned is payable on demand with the banker, e.g.

<sup>1</sup> Section 5

where he limits his right to draw cheques only upto the amount of Rs. 50/- at a time, the banker will not be bound to pay it he draws a cheque for Rs. 100/-. The banker may also refuse to pay if the drawer is a trustee in charge of a trust fund and he draws the cheque for any purpose other than that of the trust.

4. The maker of a promissory note must pay the money to the bearer at maturity if the note is payable to bearer. If the note is payable to a specific person or to his order, he must pay at maturity to the specific person or to his order.

5. The acceptor of a bill of exchange who accepts before maturity is liable to pay the amount of the bill at maturity according to the apparent tenor of the acceptance. Payment according to apparent tenor means that payment should be made to the person whose name appears on the face of the bill.<sup>1</sup> The acceptor who accepts at or after maturity must also pay according to the apparent tenor of the acceptance.

6. A negotiable instrument, we have seen, passes from hand to hand by delivery or indorsement. When such an instrument has passed a few hands all the previous holders or indorsers are liable to pay the holder for the time being in case the drawee dishonours the bill either by refusing to accept or refusing to pay after acceptance.

#### **Capacity of parties to Negotiable instrument :**

Every person capable of entering into a contract according to the law to which he is subject, may bind himself and be bound by the making, drawing, acceptance, indorsement & delivery and negotiation of a promissory note, bill of exchange or cheque.<sup>2</sup>

In India therefore all persons who are disqualified from entering into a contract such as minors, persons of unsound mind or alien enemies would not be capable of being parties to a negotiable instrument. The position of persons disqualified from entering into a contract in relation to negotiable instrument may be stated as follows —

<sup>1</sup> Section 32

<sup>2</sup> See dishonour

<sup>4</sup> Section 26 of the Negotiable Instruments Act.

**Minors :**

A minor may draw, endorse, deliver and negotiate a negotiable instrument so as to bind all parties except himself<sup>1</sup>. That is, a minor is not prohibited from being a party to a negotiable instrument, but he cannot be made liable as a party to a negotiable instrument but a negotiable instrument drawn or indorsed by a minor is nevertheless valid and all parties to the instrument excepting the minor remain liable on the instrument to the holder for the time being. A minor cannot however accept any negotiable instrument nor can he execute a promissory note. It is not clear as to whether any promissory note or bill made or drawn by a minor for necessities supplied to him is binding on him. The latter opinion seems to be that the person in whose favour the promissory note or the bill is made or drawn in such a case can sue the minor for the money on the original consideration which the minor received from him for necessities, but he cannot recover from the minor on the instrument executed by him.

**Persons of unsound mind :**

A bill or promissory note executed by a person of unsound mind whether a lunatic or a drunken person or a person who is incapable of forming a sound judgment is to the effects of such bill or note due to extreme old age or senility is not binding on such person. Such a person cannot also draw, endorse, deliver and negotiate a negotiable instrument so as to bind all parties except himself.

**Alien enemy :**

A contract with an alien enemy is void as contrary to law or public policy. Therefore a person cannot draw a bill of exchange upon the citizen of another country in war with his own country, nor can he accept a bill drawn by an alien enemy or endorse a bill or note to such an alien enemy or be a endorser from him.

**Insolvent :**

On the insolvency of a person any negotiable instrument of which he may be a holder vests in his assignee but where an insolvent has no beneficial interest in a negotiable instrument, the title to such instrument does not vest in his assignee and he may endorse a negotiable instrument accepted for his accommodation.

<sup>1</sup> See 36 of the Negotiable Instruments Act

so as to make the acceptor liable to the endorsee<sup>1</sup>. An insolvent cannot sue on a negotiable instrument nor can he pass title to such instrument by endorsement or otherwise. But if he endorses an instrument to any bona fide holder without notice, such bona fide holder acquires a valid title to the instrument so endorsed to him.

#### **Corporation :**

A corporation or company being a legal person can be a party to a negotiable instrument provided it is authorised expressly by its memorandum to do so. But even in the absence of express authority given by its memorandum a corporation may execute, endorse or accept a negotiable instrument if it is necessary and incidental to the purpose for which it was created. Such would be the case in the case of ordinary trading concerns.<sup>2</sup> If a corporation, however, exceeds its power and executes an instrument, such an instrument is void and even a bona fide holder for value cannot make the corporation liable ; for all persons dealing with a corporation is bound to ascertain its capacity to execute such an instrument. But where the power to execute instruments is given to a company by its memorandum, a person dealing with the company is not bound to enquire whether the procedure or the rules prescribed for executing such instruments by the articles have in fact been complied with. Thus where by the Articles of Association the directors of a company were empowered to authorise one of themselves to draw a bill of exchange for the company, and the managing director drew a bill without express authorisation, it was held that the company was nevertheless liable to the holder of the bill as the holder was entitled to presume that the managing director has been authorised in due course.<sup>3</sup>

We have seen before that acceptance means acknowledgement of the sum mentioned in a bill by the drawee or any other person on his behalf. Such acknowledgement is expressed by the acceptor signing his name across the bill with the word "accepted" or without it. The drawee is not liable on the bill

<sup>1</sup> Belier *vs.* Campbell, (1845) 8 Q.B. 1.

<sup>2</sup> Master of London *vs.* Charlton, 6 M. & W. 850.

<sup>3</sup> *Dick vs. Pullinger Engineering Co. Ltd.*, (1921) 1 K.B. 77.

unless the bill is presented to him for acceptance and he actually accepts it. Acceptance may be of two kinds

(1) *General Acceptance* A general acceptance means that the drawee or any other person on his behalf signs his name across the bill, with or without the word "accepted," without stipulating any condition regarding payment

(2) *Conditional or qualified acceptance* Conditional or qualified acceptance means that the drawee or any one on behalf of the drawee accepts the bill subject to a condition or qualification. The condition may relate to-

(1) the amount to be paid e.g. if the bill is drawn for Rs 1000/- the drawee may accept it for Rs 500/- only

(2) the time within which the payment is to be made e.g. if the bill is payable one month after date, the drawee may accept it as payable three months after date or as payable when the goods are sold or as payable when the drawee has funds,

(3) the place where the payment is to be made, e.g. the drawee may accept it as payable at Comilla Union Bank, Calcutta, only

The holder of a bill may refuse to recognise a qualified acceptance and treat the bill as dishonoured and sue the drawer accordingly<sup>1</sup>. But when the bill has already been negotiated and gone through several hands, the holder for the time being cannot make the drawer or any previous indorsers liable on the bill if he has agreed to a qualified acceptance without their consent. If, however, the holder obtains the consent of the drawer and his previous indorsers for such qualified acceptance he can make them liable on the bill if the drawer subsequently dishonours the bill. For example, A draws a bill on B for Rs 1000/- A indorses the bill to X, and X to Y. Y presents the bill to B for acceptance. B gives a conditional acceptance to which Y agrees without the consent of A and X. Subsequently B refuses to pay. Y cannot sue A and X on the bill. But if Y obtained the consent of A and X previous to his agreeing to the conditional acceptance, he could have sued A and X on the bill.

#### **Presentment :**

Presentment means presenting a negotiable instrument to the

<sup>1</sup> See post on dishonour

drawer, maker or acceptor thereof, for the purpose of getting payment. Presentment may be of two kinds : (1) Presentment for acceptance, and (2) Presentment for payment.

### (1) Presentment for acceptance :

Presentment for acceptance is necessary only in case of a bill of exchange payable after sight, i.e. not payable on demand or at sight. A promissory note or a cheque need not be presented for acceptance. A bill of exchange payable after sight must, if no time or place is specified therein for presentment, be presented to the drawee thereof for acceptance, if he can, after reasonable search, be found, by the drawer or any holder thereof, within a reasonable time after it is drawn, and during business hours on a business day.

*N.B.*—Business hours mean the time during which by custom or usage business is carried on and business day excludes all public holidays and also any day on which business is stopped by custom. In default of such presentment the drawee is not liable to make any payment.

If the drawee cannot, after reasonable search, be found, the bill is to be deemed as dishonoured.

If the bill is directed to the drawee at a particular place, it must be presented at that place; and, if at the due date for presentment, he cannot, after reasonable search, be found there, the bill is to be deemed as dishonoured.<sup>1</sup>

Bills payable on demand or payable in certain number of days after date, i.e., after the date on which bills which need not be presented for acceptance. A bill need for acceptance not also be presented for acceptance where (i) the drawee is a fictitious person, or (ii) the drawee cannot be found on a reasonable search, or (iii) the drawee is incompetent to contract, e.g. when he is a minor or a lunatic, or (iv) the drawee becomes insolvent or is dead.

The holder must, allow the drawee forty-eight hours Time for acceptance (exclusive of public holidays) to consider whether he will accept it where the drawee wants such a time.<sup>2</sup>

<sup>1</sup> Section 61  
<sup>2</sup> Section 63. 1. 4.

**Effect of non acceptance** When a bill is not accepted within forty eight hours of its due presentation the holder may treat it as dishonoured. The holder may also treat it as dishonoured if it is accepted conditionally.

## (2) Presentment for payment :

All promissory notes, bills of exchange and cheques must be presented for payment to the maker, acceptor or drawee thereof respectively, by or on behalf of the holder. In default of such presentment the maker or acceptor or drawee, as the case may be, is not liable to pay.<sup>1</sup> A promissory note or bill of exchange must payable at a specific period after date of sight thereof, must be presented for payment at maturity.<sup>2</sup> Presentment must be made during the usual business hours and if the drawee or acceptor or maker is a banker during banking hours and on a business day (exclusive of public holidays).

Bill, promissory notes and cheques must be presented within a reasonable time after they are received by the holder. But a promissory note is payable on demand and not payable at a specified date need not be presented at all.

*Presentment of cheques* A cheque must be presented by the holder at the bank on which it is drawn. In default of such presentment the holder cannot make the drawer liable. For example A draws a cheque for Rs 50 in favour of B. B bears on the bank manager privately that A has no money in the bank. B then opens a/c A for the amount. P cannot succeed as he never presented the cheque at the bank. Further, the holder must cash the cheque before the date on between the drawee and the maker is lost due to the prejudice of the drawer.<sup>3</sup> If the holder takes long time to present the cheque in the relation between the drawer and the banker is altered and the drawer suffers a total damage due to the delay, the drawer will not be liable if the bank fails to pay the cheque. For example, A draws a cheque in favour of B on his bank for Rs 500. At the time A has sufficient funds to meet the cheque. But B takes a long time to present the cheque.

<sup>1</sup> Section 64

<sup>2</sup> Section 66

<sup>3</sup> Section 65

<sup>4</sup> Section 72

<sup>5</sup> Section 84

and the bank fails in the meantime. Here due to B's delay A suffers loss and hence B cannot recover the money from A. But the holder can still put in his claim when the bank is wound up. But suppose at the time A drew the cheque he had only Rs 250/- in the bank. In this case A will be released from liability for Rs 250. For the remaining Rs 250/- he will still be liable to B.

### **When presentment for payment is**

A negotiable instrument need not be presented for payment in the following cases<sup>1</sup>:

- (i) Where a promissory note is payable on demand and is not payable at a specified place
- (ii) Where the maker of a promissory note or the drawee or acceptor of a bill intentionally prevents the presentation of the instrument
- (iii) Where the instrument being payable at his place of business, or at some other specified place, the maker, drawee or acceptor close such place on a business day during the usual business hours or cannot be found at such other specific place
- (iv) Where the maker, drawee or acceptor has agreed to pay even if there is no presentment
- (v) Where the maker, drawee or acceptor makes a partial payment or promises to pay in part or full after knowing that the instrument has not been presented although it has become mature or in any other way waives his right to demand presentment
- (vi) Where the drawer could not suffer damage for non-payment, the holder can make the drawer liable without presentment, e.g. where the drawer draws the bill on himself or where the drawer is a fictitious person

In cases of (ii), (iii), (iv) and (v) above the instrument is regarded as dishonoured in<sup>2</sup>; the holder can avail himself of the remedies open to him in case<sup>3</sup> of dishonour.

A negotiable instrument is said to be dishonoured when the drawee either refuses to accept it or refuses to pay. We have seen

<sup>1</sup> Section 76

<sup>2</sup> Section 64

before that only bills of exchange payable after sight have to be presented for acceptance in order to make the drawee liable. We have also seen in what cases even such bills need not be presented for acceptance. If an instrument is dishonoured, the holder must give notice of dishonour to the drawer or his previous holders if he wants to make them liable. But in certain cases such notice need not be given.

#### **Dishonour by non-acceptance :**

A bill of exchange is said to be dishonoured by non-acceptance in any of the following cases

- (a) When the drawee or one of several drawees not being partners fails to accept the bill within forty eight hours of its due presentation for acceptance.
- (b) At the instance of the holder when the drawee or one of several drawees not being partners gives a conditional acceptance.
- (c) When payment is excused and the bill remains unaccepted.<sup>2</sup>

#### **Dishonour by non-payment :**

A promissory note, bill of exchange or cheque is said to be dishonoured by non-payment when the maker of the note, acceptor of the bill or drawee of the cheque makes default in payment upon being duly required by presentment to pay the same<sup>1</sup>. We have seen before the conditions for a valid presentment for payment and also the cases where such presentment is not necessary.

#### **Dishonour by a drawee in case of need :**

The general rule is that the drawee is the only person who can accept a bill. A bill is an order on the drawee to pay the sum mentioned in the bill. The drawee by his acceptance acknowledges his liability to pay the sum. If the drawee refuses to accept, the holder can make the drawer liable on the bill. But in some cases the drawer in order to escape his liability mentions an alternative drawee to whom the holder can present the bill

<sup>1</sup> Section 91.

<sup>2</sup> For cases where presentment for acceptance is excused see ante.

<sup>3</sup> Section 92.

for acceptance in case the actual drawee refuses to accept or refuses to pay after acceptance. Such an alternative drawee is known as a *drawee in case of need*. If a *drawee in case of need* is mentioned the holder must present it to him. Otherwise the drawer cannot be made liable. A bill may be dishonoured by non-acceptance or dishonoured by non-payment in case the *drawee in case of need* also refuses to accept or refuses to pay after acceptance.

#### **Difference between dishonour by non-acceptance and dishonour by non-payment :**

In both cases the holder can make the drawer and all previous holders of the bill liable, provided he gives them notice of such dishonour. But in the case of dishonour by non-acceptance the holder has no right against the drawee as the latter is no party to the bill. He can proceed only against the drawer and all other previous indorsers. In the case of dishonour by non-payment, however, the holder can sue the drawee, as by his acceptance the drawee has already become a party to the bill.

#### **Notice of dishonour :**

When a promissory note, bill of exchange or cheque is dishonoured by non-acceptance or non-payment the holder thereof must give notice of the dishonour to all other parties whom the holder seeks to make liable thereon<sup>1</sup>. Any party receiving notice of dishonour must, in order to render any prior party liable to himself, give notice of dishonour to such party within a reasonable time. For example, A draws a bill on B for Rs. 1000/- A indorses it to X and X to Y and Y to Z. Z presents the bill to B for acceptance and B refuses. Z must notify A, X and Y if he wants to make them all liable. If he wants to make only Y liable, he must notify Y. If Y wants to make A and X liable, he must notify them and so on.<sup>2</sup>

Notice of dishonour may be given to a duly authorised agent of anyone to whom such notice should be given. It may be oral or written. If written it may be sent by post and if it is duly addressed and directed, it will operate as a valid notice, even if it is lost or miscarried. It may be in any form; but it must inform

<sup>1</sup> Section 93.

<sup>2</sup> Section 95.

the party to whom it is given, either in express terms or by reasonable intendment, that the instrument has been dishonoured, and that he will be held liable thereon; and it must be given within a reasonable time after dishonour at the place of business or residence of the party for whom it is intended<sup>1</sup>.

No notice of dishonour is necessary<sup>2</sup>.—

- (a) when it is dispensed with or waived by the party entitled thereto, e.g., when an indorser on the face of the indorsement writes "no notice of dishonour required", the indorsee can make him liable without giving him notice of dishonour;
- (b) in order to make the drawer liable when the drawer himself has put impediment in the way of payment by the drawee, e.g., when the drawer has sent wrong or damaged goods to the drawee and has thus caused difficulty to the drawee in making payment;
- (c) in order<sup>3</sup> to charge a party who could not suffer damage for want of notice, e.g., when the drawer draws a bill without sending any goods he cannot suffer any damage if notice of dishonour by the drawee is not communicated to him by the holder. In such a case the holder can make the drawer liable without giving him notice;
- (d) when the party entitled to notice cannot, after due search, be found; or the party bound to give notice is unable to give it without any fault of his own;
- (e) in order to charge the drawer when the drawer draws the bill on himself or his agent, i.e., where the acceptor is the drawer;
- (f) in case of a promissory note which is not negotiable;
- (g) when the party entitled to notice promises to pay the amount due on the instrument unconditionally after knowing the facts.

#### **Noting :**

Besides giving notice of dishonour to prior parties a holder of a dishonoured bill usually has the fact of dishonour noted down by a notary public who is a person appointed by the Central

<sup>1</sup>Section 94.

<sup>2</sup>Section 96.

Government for this purpose. The notary public notes down the following facts : (a) the fact of dishonour, (b) the date of dishonour, (c) the reason for dishonour and the reference to the notary's register<sup>1</sup>.

**Noting** serves as an authentic proof of dishonour.

### **Protest :**

When a promissory note or a bill of exchange has been dishonoured by non-acceptance or non-payment, the holder may, after having such dishonour noted as above, obtain a certificate from the notary public. Such certificate is called a protest.

When the acceptor of a bill of exchange has become insolvent, or his credit has been publicly impeached, before the maturity of the bill, the holder may, within a reasonable time, cause such facts to be noted and certified as aforesaid and such a certificate is called a *protest for better security*.

### **Discharge of parties from liability :**

In any bill, promissory note or cheque, the acceptor or the drawee or the maker or the indorser is liable for payment to the holder. This liability can be discharged in the following ways :

(a) *By payment* : All parties to a negotiable instrument are discharged when the acceptor, drawee, or maker pays the amount due, on the maturity of the instrument, to the holder. In case of an instrument payable to bearer payment to anyone in possession discharges all parties.

(b) *By cancellation* : An indorser or an acceptor is discharged from all liability to a holder, or anyone claiming under him, who cancels such indorser's or acceptor's name with intent to discharge him.

(c) *By release* : A maker, or an indorser or an acceptor is discharged from liability to a holder when the holder agrees to release or releases in any other way except by cancellation such maker, indorser or acceptor.

(d) *By default of the holder* :—(i) If the holder of a bill allows the drawee more than fortyeight hours, exclusive of public holidays, to consider whether he will accept the same, all previous parties not consenting to such

<sup>1</sup> Section 99.

allowance are thereby discharged from liability to such holder<sup>1</sup>.

- (ii) If the holder of a bill agrees to a qualified acceptance all previous parties whose consent is not obtained to such acceptance are discharged as against the holder and those claiming under him.
- (iii) If the holder fails to give notice of dishonour to all previous parties they are discharged as against the holder and those claiming under him. But the acceptor of a bill or the maker of a bill still remains liable to the holder if they are already parties to the bill.
- (iv) If the holder of a cheque fails to present it before the relation between the drawer and the banker is altered to the prejudice of the drawer and the drawer suffers damage due to such delay, the drawer is discharged of all liability to the holder.

(c) *by material alteration* — Any material alteration of a negotiable instrument while in the possession of the holder, discharges the liability of all those prior to or at the time of such alteration who do not consent to such alteration, unless it was made to carry out the common intention of the original parties. The following may be reckoned as material alterations:

- (i) alteration in date, (ii) alteration in the time of payment,
- (iii) alteration in the place of payment, (iv) alteration in the amount payable, (v) alteration in the medium and method of payment, and (vi) alteration of parties.

In some cases however, even material alterations do not discharge the liabilities of the parties to an instrument. We may state them as follows:

- (i) Alteration made before the instrument is delivered or negotiation of the instrument or before its completion.
- (ii) Alteration made in order to rectify a *bona fide* error.
- (iii) Alteration made with the consent of the parties.
- (iv) Alteration made by the way of converting an indorsement in blank into an indorsement in full.
- (v) Alteration made by way of crossing a bearer cheque.

<sup>1</sup> Section 83

<sup>2</sup> Section 86

<sup>3</sup> Section 84

### **Acceptance for honour :**

We have seen before that when a bill is dishonoured the holder can forthwith sue the drawer and all the previous parties to the bill. But when a bill has been noted or protested for non-acceptance or for better security, any person not being a party already liable thereon, may, with the consent of the holder, by writing on the bill, accept the same for the honour of any party thereto<sup>1</sup>. The purpose of such acceptance is to save the honour of any party liable on the bill and most usually to save the prestige of the drawer.

A person desiring to accept for honour must by writing on the bill under his hand declare that he accepts under protest the protested bill for the honour of the drawer or of particular indorser whom he names, or generally for honour.<sup>2</sup> Where the acceptance does not express for whose honour it is made, it shall be deemed to be made for the honour of the drawer.<sup>3</sup>

### **Liability of an acceptor for honour :**

An acceptor for honour is liable to all parties subsequent to the party for whose honour he accepts to pay in case the drawer makes default in payment.<sup>4</sup> For example A draws a bill on B. A indorses it to C and C to D and D to E and E to F. B refuses to accept the bill. Then X accepts it for honour of D. X is liable to E and F, and he can sue A and C for payment in case B refuses to pay.

A party subsequent to the one for whom the acceptor for honour accepts can claim payment from the acceptor for honour only when -

- (1) he has presented the bill to the drawee for payment after maturity, and
- (2) the drawee has refused to pay, and
- (3) the refusal has been duly noted and protested by a notary public.

### **Payment for honour :**

If a bill is dishonoured by non-payment any stranger may pay

<sup>1</sup> Section 108.

<sup>2</sup> Section 109.

<sup>3</sup> Section 110.

<sup>4</sup> Section 111.

the dishonoured bill for the honour of any party liable to pay thereon provided the bill is duly noted and protested. Such payment is known as payment for honour and any person so paying is entitled to all the rights, in respect of the bill, of the holder whom he pays.<sup>1</sup>

### **Lost or stolen Instrument and Instruments obtained by fraud or unlawful consideration :**

When a negotiable instrument has been lost or has been obtained from any maker, acceptor or holder thereof by means of an offence or fraud or for an unlawful consideration, no possessor or indorsee who claims through the person who found so obtained the instrument is entitled to receive the amount due thereon from such maker, acceptor or holder if from his privity, prior to such holder unless such possessor or indorsee is, in some person through whom he claims who is a holder the bill in due course. This means that the legal position of a possessor or indorsee of a negotiable instrument which has been lost or been obtained by means of an offence or fraud or unlawful consideration is different from that of a holder in due course under similar instances. Let us deal with all these conditions separately.

### **Lost Instruments :**

(1) When a bill or note is lost, the finder acquires no title to it against the rightful owner nor can he claim payment from the acceptor or maker. The rightful owner is entitled to get the instrument back from the finder.

(2) When the finder of a lost bill or note gets payment from the acceptor or maker who pays it *in due course* such acceptor or maker is discharged from all liability to the rightful owner but the rightful owner can always recover the money so paid to the finder.<sup>2</sup>

(3) When a bill or note which is payable to bearer or which is indorsed in blank and is therefore, transferable by mere delivery, is lost, any bona fide transferee for value without notice of the loss acquires a valid title to it and he can return the instru-

<sup>1</sup> Sections 113, 114

<sup>2</sup> Section 58

<sup>3</sup> Lowell *vs* Martin, (1813) 4 Taunt 799

<sup>4</sup> Burn *vs* Morris, (1834) 2 Cr and M 570

ment as against the rightful owner and is also entitled to payment from parties liable thereon.

(4) When the finder of a lost bill or note which is payable to order and is therefore transferable by indorsement and delivery, forges the instrument and indorses it to a *bonafide* transferee for value, the latter will not acquire any title to it for the indorser himself had no title which he could transfer, and forgery can confer no title.

(5) When a holder loses a bill he should notify all parties liable thereon about the loss.

(6) When a holder loses a bill he must apply to the drawee for payment at maturity and if the drawee refuses, he must give notice of dishonour to all the parties liable. Otherwise he will lose his remedy against the drawer and all the prior parties.

#### **Instruments obtained by means of an offence—stolen Instruments :**

A person who steals a negotiable instrument from the rightful owner cannot claim payment against anyone liable thereon and the rightful owner can always recover the instrument or the money if he has realised it from the drawee. But if he indorses it to any transferee for value who has no notice of the theft, such a *bonafide* transferee will acquire a good title not only against the thief but also against all the parties prior to him, provided the instrument was payable to bearer and as such transferable by mere delivery.<sup>1</sup>

#### **Instrument obtained by fraud :**

We have seen before that a contract becomes voidable for fraud. "So if the maker or the acceptor who is primarily liable for payment proves that the consideration for the instrument was vitiated by fraud, then the person defrauding is not entitled to recover. A bill is affected with fraud when the issue or any subsequent negotiation of it is obtained by fraud or in breach of faith. In such a case the holder of the instrument subsequent to the fraud cannot enforce payment against any party thereto, nor can he retain the bill against the true owner."<sup>2</sup> Thus, in

<sup>1</sup> *Raphael vs. Bank of England*, (1885) A.C.B. 161.

<sup>2</sup> *Bhatiyam & Adiga on Negotiable Instruments Act*, 4th ed., P. 246.

*Lewis vs. Cosgrave*<sup>1</sup> the seller of a horse obtained a cheque on the fraudulent misrepresentation that the horse was sound. It was held that there was no contract and the holder could not recover the money from the drawer. In *Baboo Lall vs. Joylall*<sup>2</sup> the plaintiff lent money on hundies to the defendant on the fraudulent misrepresentations of the latter. It was held that the plaintiff could cancel the hundies and demand repayment before the maturity of the hundies.

In the same way any holder or indorsee who claims through the person who obtained the instrument by fraud, cannot claim payment from any party liable thereon. It should be noted that the party which alleges fraud against the holder must prove it, as the presumption of law is that a holder is a holder in due course.

#### **Instruments obtained for an unlawful consideration :**

A note, bill, or cheque which is drawn for an unlawful consideration or for an unlawful object is void. In such a case the holder cannot recover any payment from any party liable on the instrument. The general rules regarding unlawful consideration or unlawful object in respect of contracts in general apply to negotiable instruments.

#### **Forged Instruments :**

"Forgery is the fraudulent making or alteration of a writing to the prejudice of another man's right. The most common species of forgery is fraudulently writing the name of an existing person. It is also a forgery to sign the name of a fictitious or a non-existing person, intending it to be believed that the instrument was signed by a real person, if the signature be placed with a fraudulent or dishonest intention."<sup>3</sup> The person who forges an instrument cannot confer a valid title even on a *bonafide* transferee for value without notice of the forgery. If the holder obtains payment on the forged instrument, the rightful owner can recover the money from him and the person who has paid the instrument can also be sued alternatively by the rightful owner for payment. For example, on a bill for Rs. 1000/-, A's acceptance to the bill is forged. The bill comes into the hands of B a *bonafide* holder for value. B acquires no title.

<sup>1</sup> (1909) 2 Taunt. 2.

<sup>2</sup> 24 Cal. 533.

<sup>3</sup> J. S. Khergandvala on the Negotiable Instruments Act 6th ed., P. 102

Where indorsement of an instrument is forged a *bona fide* transferee for value acquires no valid title where the instrument is payable to order and hence can be negotiated only by indorsement and delivery. But a *bona fide* transferee for value acquires a valid title where the instrument is payable to her and as such can be negotiated by mere delivery even though the indorsement is forged. He can retain the instrument as against the rightful owner and can enforce payment from any party liable thereon.

### **Crossed Cheques :**

To prevent anyone but the payee from cashing cheques is crossed. When a cheque is crossed no one can cash it at the counter of the bank and it must be paid to a bank.

Crossing is usually done by drawing two parallel transverse lines across the face of the cheque. There might be additional words like 'and Co' or '& Co' or 'not negotiable' written between the two parallel lines. Crossing is said to be general where there are these two parallel lines with or without the additional words.

When the crossing prescribes a particular bank, payment must be made to the bank alone. In such a case the holder must have an account with the prescribed bank or must negotiate it to a person who has such an account in order to be able to receive payment on the cheque. This type of crossing is known as *special crossing*. A special crossing need not have the two parallel lines and it may or may not contain the words 'not negotiable'.

A cheque can be crossed by the drawer or any holder subsequent to him and the crossing can be effected even if the cheque was not crossed at the time of its issue.

Whether a cheque is crossed specifically to more than one banker, the banker on whom it is drawn must refuse payment thereof.<sup>1</sup>

### **Liability of bankers :**

Where a cheque is crossed generally the banker on whom it is drawn must not pay it to anyone except to a banker and where a cheque is crossed specifically the banker on whom it is drawn must not pay it to anyone except to the banker to whom it is

crossed, or his agent for collection.<sup>1</sup> If the banker on whom a crossed cheque is drawn has paid the same in due course, i.e., in the way stated above, the banker is not liable any more to the drawer, no matter whether the payment has been received by the true owner or not. But if the banker pays the cheque in any way other than that mentioned above, he will be liable to the drawer if the latter sustains any loss owing to such payment.<sup>2</sup>

#### **Effect of crossing with the words "not negotiable" or the title to crossed cheque :**

When a crossed cheque (whether generally or specially crossed) bearing the words "not negotiable" is negotiated to any transferee for value, such transferee cannot obtain any better title than his indorser. For example, A draws a cheque and crosses it with the words "not negotiable". B, a stranger, steals the cheque and indorses it to C who takes it for value and without notice of the theft. C cannot have any valid title to the cheque as B from whom he took had no title at all.

But if a cheque is crossed without the words "not negotiable" a bona fide transferee for value acquires a valid title to it whether the person from whom he took the cheque had any good title or

#### **Hundis :**

Hundis are negotiable instruments written in the different vernacular languages of India. They are, most frequently, like bills of exchange in form and substance issued either for the purpose of financing trade or for raising loans. But they are also like promissory notes sometimes.

Hundis have been in existence in India from time immemorial and special customs and usages have been built up in respect of dealings in hundis. The Negotiable Instruments Act has not touched these customs and usages though in some important points the provisions of the Act differ considerably from such usages and customs. Thus, oral acceptance of a hundi may be recognised by courts of India if there is a local custom to that effect although the Act definitely lays down that acceptance must be in writing. Courts in India will not also insist on the notice of dishonour being given by the holder if local customs so justify although it is

<sup>1</sup> Section 126.

<sup>2</sup> Sections 128, 129

<sup>3</sup> Section 130

imperative under the Act. Hence, although hundis are not mentioned as negotiable instruments by the Act, they circulate freely as such by force of custom and usage. The rights and duties of parties in hundis are also strictly regulated by such custom and usage. But the Act lays down that the parties to a hundi may exclude the operation of such custom and usage by any words in the hundi indicating an intention that the legal relations of the parties shall be governed by the Negotiable Instruments Act.

#### Kinds of Hundis :

Hundis are mainly divided into two broad groups —

- (1) Darshani hundis, i.e., hundis payable at sight and
- (2) Muddati or Miadi hundis, i.e., hundis payable after sight or a certain time after presentation.

Darshani hundis and Muddati or Miadi hundis are again subdivided into several classes which may be mentioned as follows —

(1) *Shahjog Hundi* —It is a hundi drawn by a merchant on another merchant directing the latter to pay the hundi to a holder who must be shah, i.e., a man of substance and respectability. The drawer must take proper precautions to ascertain the respectability of the holder before he makes payment to him. Otherwise, the drawee will not be entitled to recover the money he pays out to the holder if the holder turns out to be not respectable. This type of hundi is most commonly used for the purpose of remitting money e.g. A comes to B for the purpose of remitting Rs 1000/- to C. He deposits the money with B whereupon P draws a Shahjog hundi on X directing him to pay Rs 1000/- to Shah A may send the hundi to C straightaway for C to receive the money from X. It is very rarely presented to the drawer for acceptance and most commonly it is presented for payment forthwith at the time of payment. It usually states the name of the person for whom it is drawn or who has deposited the money with the drawer. It may be either a Darshani or a Miadi hundi. It can be negotiated by mere delivery. It is very widely used in Bombay but is not so common in Bengal.

(2) *Nam jog Hundi* —It is payable to a specified person whose name is written on the face of the hundi. It differs from a Shahjog hundi in that it cannot be paid to anyone except the person who is specified or who has obtained the hundi from such a specified person by indorsement.

(3) *Dhani Jag Hundi* —It is payable to anyone who presents it *i.e.*, by any holder. It can, therefore be negotiated as an instrument payable to bearer (*Dhani* means a holder)

*Firman Jag* —It is made payable to the order of a person (*Firman* means an order)

*Dekhandar* —It is also payable to bearer or presenter

*Johmi Hundi* —It is mostly used by merchants i.e. means of insuring goods which they send to their customers or agents. For example, A in Calcutta consigns certain goods to B in Bombay. B may be either his agent or customer. A then draws a hundi on B and then sells it to C, a hundiwala whose business it is to advance the entire money minus his commission on the hundi. C or his agent in Bombay will then present the hundi to B after the goods arrive in Bombay. B may pay the hundi and take delivery of the goods. If he refuses to pay C can recover from A the money he advanced. But if the goods are lost totally C cannot recover any money from A. He must bear the whole loss. That is why these hundis are similar to insurance policies. But if the goods are only partially damaged C can recover the money from A.

#### Holder of an instrument overdue :

If the holder of an instrument acquires it when it is overdue, *i.e.* acquires it after maturity, he has only those rights against parties liable on the bill as his transferor or endorser had at the time of transfer. If his transferor could recover the money or part of the money either from the drawer or the drawee he can do the same. But if his transferor was not so entitled at the time of the transfer he cannot do so. A accepts a bill for Rs 1000/- drawn on him by B. As security for the due payment of the bill A deposits certain goods with B authorising B to sell the goods and keep the proceeds if A fails to pay. A fails to pay and B thereupon sells the goods for Rs 600/- and keeps the proceeds. B is entitled <sup>1</sup> to get Rs 400/- only from A. Subsequently B endorses the bill to X who does not know anything about the goods pledged as security. X cannot recover more than Rs 400/- from A, that being the sum which his transferor B was entitled to

<sup>1</sup> Section 59

## CHAPTER VI

### LAW OF INSOLVENCY

When a person gets so encumbered that his debts far exceed his assets, it is to the interest of the state that all his creditors get paid proportionately out of his assets and that he be allowed to get a fresh start in life. In such a case, therefore, the Law of Insolvency allows the person to be adjudged an insolvent, the effect of which is, in short, to relieve him of all liabilities and to distribute his assets most equitably for the benefit of the creditors.

#### **Acts of Insolvency :**

A person can be adjudged an insolvent only when he is a debtor and has committed an *act of insolvency*. A debtor is said to have committed an act of insolvency in any of the following cases :

(a) If he transfers all or substantially all his property to a third person for the benefit of his creditors generally, for the purpose of paying off their dues.

(b) If he transfers his property for the purpose of delaying and defeating creditors. Where he transfers his property, for value and consideration, a creditor, who alleges that the transfer was made to delay and defeat creditors, must prove so. This can be proved by the financial position of the debtor at the time of the transfer and all other surrounding circumstances. Where, however, the transfer is made by way of gift without consideration, such a gift will by itself, apart from any question of intention, constitute an act of insolvency.

(c) If he makes a transfer of any property or any part thereof which would, under this or any other enactment for the time being in force, be void as a fraudulent preference if he were adjudged an insolvent. A debtor is said to transfer property by way of fraudulent preference if he makes a transfer of property exclusively to one creditor in order to pay the latter in preference to all other creditors.

(d) If he departs or remains out of British India or from his dwelling house or usual place of business or otherwise absents himself or secludes himself, so as to deprive his creditors of the

means of communicating with him, with intent to defeat or delay his creditors

(e) If any of his property is sold or attached for a period of not less than 21 days in execution of the decree of any court for the payment of money

(f) If he petitions to the court to be adjudged an insolvent whether the petition is rejected or granted

(g) If he gives notice to any of his creditors that he has suspended or that he is about to suspend payment of his debts. mere suspension of payment is not enough, but the notice of such suspension must be communicated either verbally or in writing to any of the creditors

(h) If he is imprisoned in execution of the decree of any court for the payment of money

### Fraudulent Preference :

Fraudulent preference is hardly made a ground for adjudication of a person as insolvent. But once a person is adjudged an insolvent fraudulent preference is made a ground for avoiding a transfer of property by the insolvent prior to insolvency. The doctrine of fraudulent preference was first enunciated by Lord Mansfield in *Thompson vs Freeman*<sup>1</sup> thus 'A bankrupt, when in contemplation of his bankruptcy cannot by his voluntary act favour any one creditor. If he did so, it was regarded as a fraud and the transaction was called "Fraudulent Preference". The law was stated more lucidly in *Marks vs Eckman*<sup>2</sup> thus 'If a man at a time when he contemplates bankruptcy delivers goods or money into the hands of a creditor whom he intends to benefit, the transaction is perfectly valid between the parties; but if bankruptcy supervenes and there is an adjudication, against the transferor or donor, it is a fraudulent preference and invalid in favour of the assignees'. Under Section 56 of the Presidency Towns Insolvency Act, and Ss 54, 54A of the Provincial Insolvency Act the law, regarding Fraudulent Preference, is stated as follows. Every transfer by a debtor of his property (this includes a mortgage on a charge), every payment made, every obligation incurred, and every judicial proceeding affecting his property taken or suffered

<sup>1</sup> (1786) 1 T.R. 155

<sup>2</sup> (1870) L.R. 5 Q.B. 275, 279.

by him, is fraudulent and void against the official assignee provided five conditions are fulfilled. These conditions are :—

- (1) The debtor must at the date of transfer or payment be unable to pay from his own money his debts as they become due.
- (2) The transfer or payment must be in favour of a creditor.
- (3) The transfer or payment must, in fact, prefer one creditor over others.
- (4) The transfer or payment must have been made with a view to giving such creditor a preference over other creditors; and
- (5) The debtor must be adjudged insolvent on a petition presented within three months after the date of transfer or payment.

If any of the above conditions is not satisfied, the transaction will not be void as a fraudulent preference. Thus it is not enough to show that a creditor is preferred but it must also be shown that it was the insolvent's intention to prefer him. Even if it was, the transaction will be perfectly valid, if no insolvency petition is presented within 3 months after the date of transfer or payment.

#### **Who may be adjudged insolvent :**

The insolvency court in India has no power to adjudicate any person an insolvent unless he is a debtor and he has committed an act of insolvency. A debtor means only a debtor who is subject to the law of British India and does not mean a debtor all the world over.

#### **Foreigners :**

A foreigner cannot be adjudged insolvent by any British Indian court, unless he has committed an act of insolvency as defined in the Acts in British India. If the act was committed during the foreigner's personal residence in British India, it does not matter if he is not personally present in British India at the time of presentation of the insolvency petition. 'It is the act of insolvency and not the petition, which gives jurisdiction to a court in British India.'

### **Minors :**

It has already been observed that all agreements by a minor in India excepting agreements relating to the purchase and sale of necessaries and those for the benefit of the minors, are absolutely void. Even in the case of necessities the minor incurs no personal liability. Further a minor cannot even ratify agreements executed during his minority on his attainment of majority. It follows from this that a minor cannot, under any circumstance, be adjudged insolvent since all agreements by him for the repayment of money lent or for goods supplied are absolutely void. If a minor is adjudged in insolvent the adjudication must be annulled.

It has also been observed before that a minor cannot become a partner. But he may be admitted to the benefits of a partnership in which case his share in a partnership assets is liable for the debts of the firm. Where a firm consists of adult and minor partners only the adult partners can be adjudged insolvent and not the minor partners. If in the insolvency petition order of adjudication is sought against the firm itself, it will not be made against the firm, but it will be made against the partners of the firm other than the minor partners. In any case on the making of the order of adjudication, all the properties and assets of the firm including the minors share will vest in the Official Assignee or the Receiver.

### **Married women :**

The old common law rule that a woman could not enter into a contract during marriage without the authority of her husband has, though given up long ago. In India a married woman, whether she is a Hindu or a Mahomedan or of any other religion, enters into a valid contract and her separate properties are adjudicatable for the debts contracted by her. It follows from

it logically that in India a married woman may be adjudged for her debts and on an order of adjudication all her properties will vest in the Official Assignee or the Receiver.

**The Insolvent  
Partner of a firm :**

Under section 13, a partner may present an insolvency petition against any part

may also present a joint petition against 2 or more of them provided both or all have committed an act or acts of insolvency. But a single petition may be founded on a joint act of insolvency provided the joint act is the act of each one. Thus in order to support a joint petition against all the members of a firm it is enough if the act of insolvency is committed during the continuance of a joint debt, and the petition is founded on a joint debt. So if two persons A and B, carry on business in the firm named A. B. & Co. and debts are incurred by the firm, they are both liable to be adjudged insolvent.

✓ Under the Provincial Insolvency Act no adjudication can be made against a firm in the firm name ; it can only be made against the partners individually. This is in conformity with the English law. Under the Presidency-towns Insolvency Act<sup>1</sup>, however, an adjudication order can be made against a firm in the firm name, and such an order has the effect of adjudicating each partner insolvent. It is necessary to prove for adjudication against a firm that each of the partners must have committed some act of insolvency. If a joint act of insolvency is relied upon, it must be shown to be the act of all. Thus where one partner carries on the business of the firm and the other partners lives at a distance, and does not take any part in the business, and the partner carrying on business stops payment and departs from the place of business, it is not evidence of a joint act of insolvency against the other partners and on such evidence, no order of adjudication against the firm can be made.

#### Lunatics :

A lunatic cannot commit an act of insolvency which is ~~deliberately~~ intent such as a transfer of his property with the intent to his creditors, or departure from his dwelling house, with intent. But a lunatic can be adjudged insolvent on a de  
tracted or an act of insolvency committed prior to lunacy in British England if a person is found a lunatic by inquisition and commits an act of insolvency (such as where the lunatic's property is committed in the hands of the committee appointed by the Court in Lunacy, it does not have to be attached for 21 days), the Court in Lunacy grants a power to the Committee in the name of the lunatic to consent to the act of to a court

<sup>1</sup> Section 99.

of adjudication against the lunatic or to present a bankruptcy petition in the name of the lunatic, if it is for the benefit of the lunatic to do so. The same principle, it is submitted, applies in India.

#### **Joint Debtors :**

If two or more persons contract a joint debt and the joint debt is not satisfied by either or both of them, the creditor may present a single insolvency petition, against the joint debtors provided they have each committed some act of insolvency. The act of insolvency may be a joint act provided it is shown to be the act of all. Thus if the creditor obtains a decree against the joint debtors and property jointly belonging to the debtors has remained under attachment for a period of 21 days, the creditor may present a single insolvency petition against all the debtors. But if the property attached belongs only to some of the debtors and not to all, then the debtors who have no interest in the property attached cannot be adjudged insolvent on the petition, since they cannot be deemed to have committed an act of insolvency.

#### **Joint Hindu Family :**

A joint Hindu family cannot be adjudged insolvent. But the members of a Joint Hindu family may be declared insolvent on a single petition by a creditor provided they are personally liable on a joint debt and have committed an act of insolvency, e.g., by jointly transferring family property to a creditor by way of fraudulent preference. But it should be noted that where the business of a joint Hindu family is carried on by the manager of the family and debts are contracted by him, in the course of business, the shares of the other members in the family business only are liable for such debts and they are not personally liable for the same. Therefore, they can never be adjudged insolvent on such debts. It should also be noted that in no case can a minor be adjudged insolvent.

#### **Companies :**

Registered companies can never be adjudged insolvent under the Insolvency Acts. In case the creditors of the company desire to have the company adjudged insolvent, they should proceed under the winding up provisions of the Indian Companies Act, 1956.

**Proceedings consequent on order of adjudication :**

When an order of adjudication is made against a debtor, the following are the usual proceedings after the adjudication order under the Presidency-towns Insolvency Act<sup>2</sup>:

(1) The debtor is required to prepare and submit to the Court a schedule in relation to his affairs in such form and containing such particulars as may be prescribed, verified by an affidavit within 30 days of the order when the order is made on a petition by the debtor or within 30 days from the service of the order when the order is made on the petition of a creditor. If the debtor fails to submit the schedule within due date without reasonable excuse, he may be committed to civil prison and the Official Assignee may have the schedule prepared at the expense of the insolvent's estate.

(2) Any insolvent who has submitted his schedule may apply to the court for an order protecting him from commitment to civil prison for failure to pay any debt owed by him and the Court may make an order preventing the insolvent from arrest or detention. The Court usually makes such an order where it finds that it produces a certificate from the Official Assignee that he has so far conformed to the provisions of the Act.

The Court may order the Official Assignee to summon a meeting of the creditors of the insolvent on the application of a creditor or of the Official Assignee for the purpose of considering the circumstances of the insolvency and the insolvent's schedule and his explanation thereon and generally as to the mode of dealing with the property of the insolvent.

(4) Where an order of adjudication is made, the court is required to appoint a day, for the public examination of the insolvent, as soon as conveniently may be after the expiration of the time for the filing of the insolvent's schedule. At such public examination any creditor may question the insolvent regarding his affairs.

<sup>2</sup> Sections 24, 27, 33-37.

and the causes of his inability to pay his debts. The Official Assignee must be present and the Court may put such questions to the insolvent as it thinks fit.

- (5) The insolvent must, unless there is a reasonable excuse, attend the meeting of the creditors which the Official Assignee may require him to attend and furnish such information as the meeting may require and also answer all queries in public examination. He must also do all that the official assignee may require him to do such as giving an inventory of his property, a list of his creditors and debtors and so on.
- (6) The court may order the arrest of an insolvent and commit him to civil prison if it appears that the insolvent has absconded or is about to abscond with a view to avoiding public examination or deferring insolvency proceedings or is about to remove his property or is, in any other way trying to hamper insolvency proceedings.
- (7) The court may, on the application of the Official Assignee or of any creditor who has proved his debt, order any person known or suspected to be in possession of any property belonging to the insolvent or supposed to be indebted to the insolvent or may be deemed capable of giving information respecting the insolvent, his dealings or property and/or may require him to produce any document in his custody or power relating to the insolvent, his dealing or property.
- (8) If the person who appears is above admits that he is indebted to the insolvent or that he is in possession of any property belonging to the insolvent the court may order him to pay to the Official Assignee the amount of which he is indebted or to deliver the property of the insolvent which is in his possession to the Official Assignee.

The following are the proceedings consequent on an order of adjudication under the Provincial Insolvency Act<sup>1</sup>:

- (1) Any insolvent after he has been adjudicated insolvent, may apply to the court for protection as under the

<sup>1</sup> Sections 31, 33, 59A.

Presidency-towns Insolvency Act, and the court may make an order for his protection from arrest or detention.

- (2) After an order of adjudication all persons who claim to be creditors of the insolvent in respect of debts provable under the Act must tender proof of their respective debts by producing evidence of the amount and particulars thereof and the court shall, by order determine the persons who have proved themselves to be creditors of the insolvent in respect of such debt and the amount of debts, respectively, and shall frame a schedule of such persons and debts.

#### **Proof of Debts :**

It has already been observed that when a person is adjudged insolvent, all his properties vest in the Official Assignee or the Receiver, and his creditors are deprived of the ordinary legal remedies against the insolvent for the recovery of their debts. But the creditors acquire the right to share equally and proportionately in the distribution of the insolvent's assets.<sup>1</sup> A creditor who wishes to share in the distribution must prove for his debt in the mode prescribed by the Act. The debts however, must be such as are provable in insolvency. Debts and liabilities in respect of which creditors are entitled to share in the distribution of the assets are called debts 'provable in insolvency' and the method by which debts and liabilities are established is called 'proof of debts'. A creditor who fails to prove for a debt liability which is provable in insolvency cannot, after the discharge of the insolvent, sue him for it.

#### **Debts provable in insolvency :**

All debts and liabilities present or future, certain or contingent, to which the debts of subject when he is adjudged insolvent or to which he becomes subject before his discharge by reason of any obligation incurred before on date of such adjudication, shall be deemed to be debts provable in insolvency save and except the following:

- (1) Demands in the nature of unliquidated damages arising

<sup>1</sup> Pres towns Insolvency Act, Sec 46, Prov Insolvency Act, Sec 34

otherwise than by reason of a contract or breach of trust. These are demands which a person may make on another for tort such as defamation, assault, malicious prosecution, and so on. If, however, such demands have crystallised into liquidated damages, by virtue of a decree passed against the insolvent, such damages may be proved in insolvency.

- (2) Debts or liabilities contracted by the debtor with any person who has had notice of the presentation of any insolvency petition by or against the debtor, cannot be proved in insolvency. This, however, does not apply to cases of insolvency under the Provincial Insolvency Act, and as such a debt or liability of this type is provable under that act.
- (3) Debts and liabilities the value of which cannot be, in the opinion of the court, fairly estimated.
- (4) Debts which are against public policy are not provable, such as a debt which is founded on illegal and immoral consideration, or an agreement to pay money to a creditor to induce him not to oppose the debtor's discharge from insolvency which is a fraud on the insolvency laws.

#### **Proof of Debts :**

The rules of proof of debts under the Presidency-towns insolvency act are contained in Schedule II of the Act and are as follows :

- (1) *Time for lodging proof.*—Every creditor shall lodge the proof of his debt as soon as may be after the making of an order of adjudication. (R. I.)
- (2) *Mode of lodging proof.*—A proof may be lodged by delivering or sending by post in a registered letter to the Official Assignee an affidavit verifying the debt. The affidavit may be made by the creditor himself or by some persons authorised by or on behalf of the creditor. If made by a person so authorised, it shall state his authority and means of knowledge. The affidavit shall contain or refer to a statement of account showing the particulars of debts and shall specify the voucher, if any, by which the same can be substantiated. The Official Assignee may, at any time, call for the

production of the voucher. The affidavit must also state whether the creditor is or is not a secured creditor (R 2, 3, 4 and 5).

- (3) *Cost of proving debt.* A creditor must bear the cost of proving his debt unless the court otherwise specially orders (R 6).
- (4) *Right to examine proof.* Every creditor who has lodged the proof shall be entitled to see and examine the proofs of other creditors at all reasonable times (R 7).

Rules as to proof of debt under the Provincial Insolvency Act (S 49) are the following:

- (1) A debt may be proved by delivering or sending by post in a registered letter to the court an affidavit verifying the debt.
- (2) The affidavit shall contain a reply to a statement in account showing the particular of the debt and shall specify the voucher (if any) by which the same can be substantiated. The court may at any time call for the production of the voucher.

#### **Proof by secured creditors:**

A secured creditor stands outside insolvency proceedings. He can proceed in the ordinary course of law to realise his security. If he is a mortgagee and by the mortgage deed he is given the power to sell the mortgaged property without the intervention of the court he may have the property sold even if the mortgagor becomes insolvent and appropriate the proceeds of sale in payment of his dues. The surplus if any is transferred to the Official Assignee or Receiver. If however he has no power to sell the mortgaged property he can bring a suit for sale of the mortgaged property and have the same sold by a decree of the court. But a secured creditor may come into insolvency proceeding and he does so usually where the security proves insufficient for his debts. If he comes under the insolvency, he has the following three courses open to him, viz.

- (1) He may realise the security and then prove for the balance.
- (2) He may surrender his security and prove for the whole debt.

- (3) He may state in his proof the value at which he assesses his security and prove for the balance after deducting the assessed value.
- (4) Under the Presidency-towns Insolvency Act, Sch. II, rr. 18-21 a mortgagee of any part of the insolvent's real or leasehold estate may apply to the court for proving his mortgage and on such application the court must proceed to enquire whether such person is such mortgagee, and for what consideration and under what circumstances ; and if it is found that such person is such mortgagee, the court must direct such accounts and enquiry to be taken as may be necessary for ascertaining the principal, interest and cost due upon such mortgage and if the court is satisfied that there ought to be sale, the court must direct the notice of such sale to be advertised and the Official Assignee shall have the conduct of such sale. The proceeds of sale will be applied in the first instance for the satisfaction of the mortgagee's dues and cost and the surplus, if any, is to be transferred to the Official Assignee.

#### **Properties of the insolvent :**

We have already seen that as soon as a debtor is adjudged an insolvent, all his properties vest in the Official Assignee or the Receiver for the benefit of his creditors, who are entitled to share proportionately. But the question is 'What is the property of the insolvent?' In both the Acts the property of the insolvent means such of his property as is divisible amongst his creditors. We have, therefore, to examine what properties are divisible and what are not divisible.

Under the Presidency-towns Insolvency Act<sup>1</sup>, the following are not divisible amongst creditors :—

- (1) Property held by the insolvent on trust for any other person.
- (2) The tools, if any, of his trade and the necessary wearing apparel, bedding, cooking vessels and furniture of himself, his wife and children, to a value, inclusive of

<sup>1</sup> Section 52.

tools and apparel and other necessaries as aforesaid, not exceeding Rs. 300/- in the whole.

Under the same act the following have been held to be divisible amongst the insolvent's creditors.

- (a) All such property as may belong to or be vested in the insolvent at the commencement of the insolvency or may be acquired by or devolve on him before his discharge.
- (b) The capacity to exercise and to take proceedings for exercising all such powers in or over or in respect of property as might have been exercised by the insolvent for his own benefit at the commencement of his insolvency or before his discharge.
- (c) Goods in the possession, order or disposition of the insolvent in his trade or business by the permission of the true owner under circumstances that he is the reputed owner thereof.

Under the provincial Insolvency Act,<sup>1</sup> the following are held divisible amongst the insolvent's creditors.

- (i) All goods being at the date of the presentation of the insolvency petition, in the possession of the insolvent, by the consent and permission of the true owner under such circumstances that he is the reputed owner thereof.
- (ii) All properties which are acquired by or devolve on the insolvent after the date of the order of adjudication and before his discharge.

Under the same act such property as is exempted by the Code of Civil Procedure or any other enactment from liability to attachment and sale in execution of a decree are not divisible amongst the creditors of the insolvent. It should be noted that under section 60 of the Civil Procedure Code articles similar to those mentioned in clause 2 above as not divisible under the Presidency-towns Insolvency Act, are exempt from attachment and sale.

#### **Onerous property :**

Under the Presidency-towns Insolvency Act,<sup>2</sup> the Official

<sup>1</sup> Section 28.

<sup>2</sup> Sections 62-67.

Assignee has a right to disclaim or get rid of onerous property. This power to disclaim is an exception to the general rule that the Official Assignee takes the estate of the insolvent subject to all the claims in law and equity to which it was subject in the hands of the insolvent. Onerous property has been defined by Section 62 of the Presidency towns Insolvency Act as consisting of land or any tenure burdened with onerous covenant, shares or stocks in companies, unprofitable contracts or any other property that is unsaleable, or not readily saleable, by reason of its binding the possessor thereof to the performance of any onerous act or in the payment of any sum of money. The Official Assignee, if he wants to disclaim, must do so in writing signed by him. The time allowed to the Official Assignee for such disclaimer is 12 months after the insolvent has been adjudged insolvent or where the property came to the knowledge of the Official assignee more than one month after such adjudication, 12 months after he first came to know of it.

#### **Reputed ownership :**

It has already been seen that all the property of which the insolvent is the true owner at the commencement of the insolvency vests in the Official Assignee or the Receiver. But in case of goods, i.e., moveable property it is not only the goods of which the insolvent is the true owner at the commencement of the insolvency, but also goods which are the property of other people but of which the insolvent is the apparent or reputed owner, which vests in the Official Assignee or the Receiver. Thus if a person buys goods from a trader and pays for them, but suffers the goods to be kept by the seller in his possession and the seller subsequently becomes insolvent, the goods will generally vest in the Official Assignee and will be divisible for the benefit of the insolvent's creditors. In such a case the insolvent is deemed to be the reputed owner of the goods. The principle is that the buyer in this case, though he is the true owner must suffer, because he helps the insolvent to obtain false credit by allowing the goods to remain with him. It should be noted that the following conditions must be satisfied to enable the Official Assignee or the Receiver to claim a property of the insolvent under the reputed ownership clause:

- (a) The property claimed must not be immoveable property but goods

- (b) The goods must be in the possession, order or disposition of the insolvent in his trade or business at the commencement of the insolvency. Goods not used for the insolvent's trade or business do not pass to the Official Assignee. Thus household furniture belonging to others but lying at the private residence of a trader who becomes insolvent do not pass to the Official Assignee or Receiver.
- (c) The goods must be in possession of the insolvent under such circumstances that he is a reputed owner thereto. Thus in *Greening v. Clark*<sup>1</sup>, the facts were as follows. A buys certain goods from B and pays the price to B. A leaves the goods with B who pledges them with C. C sells the goods on default of payment by B, and certain surplus is left in the hands of C out of the sale proceeds after the satisfaction of C's claim. B afterwards becomes bankrupt and the surplus is claimed both by A and the trustee in bankruptcy. It was held that the goods were not in the possession of the bankrupt and the surplus must pass to A.
- (d) The true owner must consent to the possession of goods by insolvent and to the possession thereof in the insolvent's trade or business under such circumstances that the insolvent is the reputed owner of the goods.

#### **Realisation of the property of the insolvent :**

Under the Presidency towns Insolvency Act the Official Assignee must take possession as soon as possible of the deed books and documents of the insolvent and of all other parts of his property capable of manual delivery. For this purpose any treasurer or other officer, or any banker, attorney or agent of the insolvent, is bound to pay and deliver to the Official Assignee all money and securities in his possession or power in his particular capacity. In default he is punishable for contempt of court. The court may also issue a warrant to any prescribed officer of the court or any police officer above the rank of a constable to seize any part of the property of the insolvent in the custody or possession of the insolvent or of any other person. The Official Assignee

may also summon any person known or suspected to be in possession of any part of the insolvent's property and may require him to deliver such property if the Official Assignee is satisfied that he is, in fact, in such possession.

But if the insolvent has sold his book debts and delivered his books of accounts to a purchaser, the Official Assignee cannot claim the books. The Official Assignee cannot also ask for delivery of books belonging to the insolvent and other or others jointly, though he is entitled to inspect the same.

Under the Provincial Insolvency Act the court has authority to remove a person from the possession of the insolvent's property and the Receiver can always take possession of the property of the insolvent.

Under both the acts certain powers are conferred on the Official Assignee or the Receiver to enable them to realise the property of the insolvent. Some of the powers are exercisable without the leave of the court and some can only be exercised with the leave of the court.

#### **Powers exercisable without the leave of the court :**

The following powers may be exercised by the Official Assignee or the Receiver without the leave of the court:

(1) He may sell any or all the property of the insolvent by public auction or by private treaty.

(2) He may give receipts for any money received by him.

The following are the powers which may be exercised by the Official Assignee or the Receiver with the leave of the court.

(1) He may carry on the business of the insolvent so far as may be necessary for the beneficial winding up of the same and for no other purpose.

(2) He may institute defend, or continue any suit or legal proceedings relating to the property of the insolvent and for that purpose employ a legal practitioner.

(3) The Official Assignee may accept as the consideration for the sale of any property of the Insolvent a sum of money payable at a future time or fully paid up shares, debentures or stock, subject to such stipulations as to security and otherwise as the court thinks fit under the Presidency towns Insolvency Act Under the Provin-

and Insolvency Act the Receiver can accept only money payable at a future time and nothing else

- (4) He may mortgage or pledge the insolvent's property for raising money for the payment of his debts. Under the Presidency-towns Insolvency Act the Official Assignee may do the same for the purpose of carrying on the business also.
- (5) He may refer any dispute to arbitration, and compromise all debts, claims and liabilities on such terms as may be agreed upon
- (6) He may divide in its existing form amongst the creditors, according to its estimated value, any property which from its peculiar nature or other special circumstances, cannot readily or advantageously be sold

#### **Distribution of the property :**

In distributing the property of the insolvent, the following debts must be paid before any others —

- (1) Debts due to the Crown or to any local authority
- (2) Salary or wages of any clerk, servant or labourer in respect of services rendered to the insolvent during 4 months before the presentation of the petition, not exceeding Rs 300/- for such clerk and Rs 100/- for each such servant or labourer, and under the Provincial Insolvency Act the salary or wages, not exceeding Rs 20/- in all of any clerk, servant or labourer, in respect of services rendered to the insolvent during 4 months before the date of presentation of the petition
- (3) Rent due to a landlord from an insolvent, not exceeding one month's rent under the Presidency towns Insolvency Act only

The above mentioned debts rank equally between themselves and must be paid in full if the assets are sufficient. If the assets are insufficient they share in equal proportion between themselves.

After the preferential debts mentioned above are satisfied in full, all debts which are entered in the schedule are to be paid rateably according to their respective amounts and they shall rank equally. If the debts are paid in full, the surplus assets, if any, are to be applied in payment of interest on the debts at 6% per annum from the date of the order of adjudication.

In the case of insolvency of partners, the usual rule is that the partnership property is applicable in the first instance in payment of the partnership debts, and the separate estate of each partner is applicable in the first instance in payment of the separate debts. In case of a surplus from the separate estate of the partner, the surplus is to be applied for the satisfaction of the partnership debts. And if there is a surplus of the partnership property, the same is to be applied for the satisfaction of the separate debts of the partners in proportion to their respective shares.

### **Protected transactions :**

Protected transactions mean those transactions by an insolvent with a third party which cannot be impeached by the Official Assignee or Receiver after the order of adjudication. Transactions or dealings by a debtor in respect of his property fall into three classes :—

1. Dealings before the commencement of the insolvency proceedings.
2. Dealings between the commencement of the proceedings and the date of the order of adjudication.
3. Dealings after the order of adjudication.

As regards the first class of dealings no transfer of debts, by a debtor before the commencement of his insolvency proceedings can be impeached unless such transfer is without any <sup>intention</sup> in such form as by way of fraudulent preference.

As regards the second class of dealings property by his wilful are *bona fide* and if the person who deals with correct his property to notice at the time of the presentation of an *insolvency petition* to make good by or against the debtor. any loss so occasioned

As regards the third class of transactions protected in any case and the question arises if an insolvency petition does not arise.

If the above acts of insolvency, **Official Assignee & Receiver** ; an insolvent can be presented

**Appointment.**—The Chief debtor himself.

of Judicature at Fort William against the debtor only if— and the Judicial Commissioner the debtor to the creditor or where appoint substantively or to more than one creditor jointly petition, to the office of the Official Receiver the debt due to these creditors jointly in case of other courts a sum amount to at least Rs. 500/- and estate on the making of an ascertained or a liquidated sum, i.e., not

Assignee and every Receiver is to give security as may be prescribed by the rules or in the case of a receiver, as the court may direct. The Local Government may appoint official Receiver to be receivers under the Provincial Insolvency Act within such local limits as it may prescribe. In such a case in the absence of any exceptional reasons such as personal disqualification affecting the Official Receiver he alone should be appointed receiver in insolvency.

### Duties and powers of Official Assignee :

The Official Assignee must furnish security as may be prescribed by the rules. He may administer oaths for the purpose of affidavits, verifying proofs, petitions or other proceedings in insolvency. He has duties in relation to the conduct of the insolvent as well as to the administration of his estate. In particular it is his duty to investigate the conduct of the insolvent ~~Dir~~ to report to the court upon any application for discharge,

In whether there is reason to believe that the insolvent has debts m<sup>is</sup> an act which constitutes an offence under the Act or

(1) L<sup>21-424</sup> of the Indian Penal Code, in connection with

(2) S<sup>y</sup> or which would justify the court in refusing, resp qualifying an order for his discharge and to make 4 m<sup>rt</sup> concerning the conduct of the insolvent as the exceed or as may be prescribed and to take such part such s<sup>t</sup>ance in relation to the prosecution of any Insolvency<sup>s</sup> the court may direct or as may be prescribed.

Rs. 20/- sh<sup>l</sup> any creditor on demand and on payment of service<sup>e</sup> a list of creditors showing the amount of before the<sup>l</sup> may sue and be sued by the name of 'The

(3) Rent due to property of an insolvent'. Subject to any insufficiency<sup>l</sup> Official Assignee must, in the adminis-  
Insolvency Act<sup>l</sup> the property of the insolvent, have

The above-mentioned debt<sup>l</sup> may be passed by the creditors at and must be paid in full if the<sup>l</sup> on meetings of the creditors for are insufficient they abate in equal<sup>l</sup> summon meetings of the

After the preferential debts me<sup>w</sup> whenever requested in writing full, all debts which are entered in creditors who have approved. rateably according to their respective a<sup>u</sup>ally where he indulges in equally. If the debts are paid in full, iects a proof unreasonably are to be applied in payment of interest Court for directions in am<sup>u</sup>um from the date of the order of adj<sup>u</sup> under the insolvency. th the discretion of the

Official Assignee at the instance of a creditor unless he does something, which is so utterly absurd that no reasonable man could do it. He should also keep his account correctly and accurately and must account to the Court and pay over all moneys and deal with securities as may be prescribed by the rules. The court may also call the Official Assignee to account for any misfeasance, neglect or omission which may appear in his account or otherwise, and may require him to make good any loss, which the estate of the insolvent may have sustained by reason of his misfeasance, neglect or omission.

#### **Duties and powers of Receiver :**

The Receiver must furnish security required of him. He must take the necessary steps for the discovery of the insolvent's property, to realise the property and to distribute it amongst the creditors. He may also make a report on the conduct of the insolvent. Where the Official Receiver is appointed the Receiver in insolvency, the High Court with the sanction of the Government may, from time to time, direct that subject to the supervision of the High Court, the Receiver will have the following powers : (a) To frame schedules and to admit or reject proof of debts, (b) to make interim orders where necessary, and (c) to hear and determine any unopposed or ex parte application. Where a receiver fails to submit his account at such periods and in such form as the Court directs, or fails to pay the balance due from him thereon as the court directs or occasions loss to the property by his wilful default or gross negligence, the court may direct his property to be attached and sold and may apply the proceeds to make good any balance found to be due from him or any loss so occasioned by him.

#### **Petition for adjudication :**

If a debtor commits any one of the above acts of insolvency, a petition for adjudicating him an insolvent can be presented either by a creditor or by the debtor himself.

A creditor can petition against the debtor only if—

- (a) the debt owing by the debtor to the creditor or where Creditor's Petition. more than one creditor jointly petition, the debt due to these creditors jointly amount to at least Rs. 500/-, and
- (b) the debt is an ascertained or a liquidated sum, i.e., not

a debt whose amount is not fixed or whose amount has to be fixed or ascertained by the court, and

- (c) the act of insolvency for which the petition has been presented has been committed not more than three months before the petition is presented

A debtor is entitled to present an insolvency petition if (a) Debtor : his debt's amount to at least Rs 500/- or (b) he Petition : has been imprisened or imprisoned in execution of a decree or (c) his property has been attached under such a decree.

Under the Presidency Towns Insolvency Act the High Courts of Calcutta Madras Bombay and the Chief Court Courts of Sind can entertain insolvency petitions Under the Provincial Insolvency Act the district courts can also entertain insolvency petitions.

A court cannot entertain an insolvency petition unless the debtor is imprisoned for debt or resides or carries on business within the court's jurisdiction.

#### **Effect of an order of adjudication :**

If on an insolvency petition a debtor is adjudged an insolvent, the order of adjudication has the following effects

(1) Under the Presidency Towns Insolvency Act all the property of the insolvent, whether movable or immovable, wherever situated vests in the Official Assignee and becomes divisible among his creditors. Under the Provincial Insolvency Act all the property of the insolvent vests in the court or in a Receiver who may be appointed by the court at the time of the order of adjudication or at any time after it.

(2) All creditors whose debts may be proved to the official assignee or the Receiver are barred from instituting any suit against the insolvent without the leave of an insolvency court, during the pendency of the insolvency proceeding, i.e. during the time the debtor remains insolvent. If any suit is instituted without obtaining such leave the court in which the suit is instituted may, on proof that in order of adjudication has been made against the debtor, either stay it or allow it to continue. But the court must not allow it to continue unless there are special circumstances, e.g. that the suit was ripe for hearing at the time of insolvency, or that the suit if stayed would be barred.

by limitation or that the evidence whereby the debt is to be proved will be lost if the suit is stayed, and so on. But the right of a secured creditor, i.e., a creditor whose debt is secured by mortgage, pledge or hypothecation, to institute a suit is not barred.

(3) The insolvent is deprived of all powers to enter into transactions which will bind his creditors in respect of his property. After adjudication the Official Assignee or Receiver alone is entitled to deal with the insolvent's property and he alone can give a title to a purchaser. If a person pays a sum of money, which he owed to the insolvent, after the order of adjudication, he will have to pay it again to the Official Assignee or Receiver. If, after adjudication, a person buys property from the insolvent, he acquires no title to it.

(4) An insolvent until he is discharged suffers under certain disabilities, e.g., incapacity to hold certain offices like that of a magistrate or a member of a local authority. But the disqualifications cease if the order of adjudication is annulled.

(5) Any transfer of property, not made for valuable consideration or before or in consideration of marriage, made by the insolvent within two years before the order of adjudication will not bind the Official Assignee or may be annulled by the court at the instance of the Official Receiver.

(6) Any transfer of property made by the insolvent within three months before the order of adjudication, with the intent of benefiting one creditor at the expense of other creditors, will be void as fraudulent preference.

#### **Discharge of an insolvent :**

An insolvent may at any time after the order of adjudication apply to the court for an order of discharge and the court is required to appoint a day for the hearing of the application. On the day of the hearing the application is heard in public. The court hears the report of the official assignee or the receiver about the conduct and affairs of the insolvent. The court may also hear the debtor and the creditors. The court may, after hearing all the facts, make any of the following orders :

- (1) Discharge the insolvent unconditionally.
- (2) Refuse the discharge.
- (3) Suspend the discharge for a specified time.

(4) Suspend the discharge until a dividend of not less than four annas in the rupee has been paid to the creditors.

(5) Discharge the insolvent conditionally, e.g., on condition that the insolvent undertakes to pay unsatisfied debts after his discharge.

But a court will not grant an absolute discharge under the following conditions :

(1) Where the insolvent has committed offences under S. 103 of the Pr. Towns Insolvency Act and under S. 421 to 424 of the Indian Penal Code. (S. 103 of the Pr. T. In. Act relates to fraudulent concealment of the insolvent's state of affairs by destruction of documents, keeping false books and so on).

(2) Where the assets of the insolvent are not as required by the Pr. T. In. Act, equal to four annas in the rupee, and as required by the P. In. Act, equal to eight annas in the rupee, on the amount of his unsecured debts, unless the insolvent satisfies the court that this is due to misfortune and not to his fault.

(3) Where the insolvent has failed to keep such book, of account as is usual and proper in the business carried on by him and as should fairly disclose his financial position within three years immediately preceding his insolvency.

(4) Where the insolvent has continued to trade knowing himself to be insolvent.

<sup>for - 1</sup>nowing  
vency. Art.

(5) Where the insolvent contracted debts which he had not any reasonable expectation to be able to pay at the time. It is the contracting of debts which is made an offence and not the obtaining of goods without any reasonable expectation to be able to pay.

(6) Where the insolvent has failed to account satisfactorily for any loss of assets or for any deficiency of assets to meet his liabilities.

(7) Where the insolvent has brought about his insolvency by rash or hazardous speculations or by extravagance or by gambling or by neglect of his business affairs.

(8) Where the insolvent has caused unnecessary expenses to his creditors by putting frivolous or vexatious defence to any suit brought by such creditors.

(9) Where the insolvent has within three months preceding the time of presentation of the petition, incurred unjustifiable expense by bringing a frivolous or vexatious suit.

(10) Where the insolvent has, within three months preceding the presentation of the petition, given an undue preference to any of his creditors.

(11) Where the insolvent had been adjudged an insolvent previously.

#### **Effect of an order of discharge :**

An order of discharge releases the insolvent from all debts payable in insolvency except the following :

- (1) any debt due to the Crown; or
- (2) any debt or liability incurred by means of any fraud or fraudulent breach of trust to which he was a party ; or
- (3) any debt or liability in respect of which he has obtained forbearance by any fraud to which he was a party ; or
- (4) any liability under an order for maintenance made under S. 488 of the Code of Criminal Procedure i.e. maintenance ordered by a Magistrate on a person who neglects to maintain his wife and children inspite of having sufficient means.

## CHAPTER VII

### ARBITRATION

"A *reference* or *submission* to arbitration is an agreement made by two or more parties between whom some difference has arisen, or may thereafter arise, whereby they appoint another person or persons to adjudicate upon such difference, and agree to be bound by his decision thereon. The person appointed to adjudicate upon the difference is called an *Arbitrator*. Where two arbitrators are appointed and the submission provides that in the event of their disagreement, the matter in dispute shall be referred to the decision of a third person, such third person is called an *Umpire*"<sup>1</sup>. The decision of the arbitrator or arbitrators is called an *award*. The object of arbitration is the final disposition, in a speedy and inexpensive way, of a dispute between two parties so that they may be saved the delay and expense of litigation in a court of law.

A reference or submission to arbitration may take place in three ways :

- (1) By agreement between the parties without the intervention of the court; or
- (2) Through the intervention of the court ; or
- (3) By the operation of statutes.

Let us discuss each of these ways separately.

#### **Arbitration without intervention of the court :**

Sec. 2(a) of the Indian Arbitration Act of 1940 defines an arbitration agreement as a written agreement to submit present or future differences to arbitration, whether an arbitrator is named therein or not. Such an agreement is also known as a *submission*, a term which the Indian Arbitration Act of 1899 used. In every agreement for arbitration or submission the following terms are implied unless the parties provide otherwise<sup>2</sup>.

1. The reference or submission is to a sole arbitrator unless otherwise expressly provided.

<sup>1</sup> *Halsbury on Arbitration* Vol. I, p. 439.

<sup>2</sup> Section 3.

2 If the reference is to an even number of arbitrators the arbitrators shall appoint an umpire not later than one month from the latest date of their respective appointments

3 The arbitrators must make their award within four months after entering on the reference or after having been called upon to act by notice in writing from my party to the arbitration agreement or within such extended time as the court may allow

4 If the arbitrators have allowed their time to expire without giving an award, or have delivered to my party to the arbitration agreement or to the umpire a notice in writing that they cannot agree, the umpire shall forthwith decide on the reference in lieu of the arbitrators

5 The umpire must make his award within two months of entering on the reference or within such extended time as the court may allow

6 The parties to the reference and all persons claiming under them must submit to examination by the arbitrators and produce before them all documents and papers relating to the dispute in question and do all other things which, during the proceedings on the reference, the arbitrators or umpire may require

7 The award shall be final and binding on the parties

8 Costs of the reference and the award will be borne by the parties as the arbitrators may in their discretion direct

#### **Appointment of arbitrators : / 47/ )**

An arbitrator or arbitrators are appointed in the following ways

(1) The parties to an arbitration agreement may provide that the arbitrator or arbitrators will be appointed by consent of the parties. In such a case the parties appoint the arbitrator or arbitrators. But if the parties do not, after differences have arisen, agree to the appointment or appointments, or if my appointed arbitrator or umpire neglects or refuses to act, or is incapable of acting, or dies, and the parties do not supply the vacancy, or if the parties or the arbitrators are required to appoint an umpire and do not appoint him, any party may serve the other parties with a written notice to concur in the appointment or appointments or in supplying the vacancy. If the appointment is not

made within fifteen clear days after the service of the said notice the court may on the application of the party who gave the notice and after giving the other parties an opportunity of being heard appoint an arbitrator or arbitrators or an umpire, as the case may be, who shall have power to act in the reference and to make an award<sup>1</sup>.

(2) The parties to a submission may agree that the arbitrator or arbitrators will be appointed by a person designated in the agreement, either by name, e.g., Sir N. N. Sircar or Sir P. C. Roy, or as the holder for the time being of any office or appointment, e.g., the President of the Bengal Chamber of Commerce or the President of the Bengal Legislative Assembly and so on.

#### **Removal of arbitrators :**

Arbitrators cannot be removed except with the leave of the court, unless the parties had reserved the right of revoking the authority of the arbitrators. The court may, on the application of any party to a reference, remove an arbitrator or umpire who fails to use all reasonable dispatch in entering on and proceeding with the reference and making an award or who has misconducted himself or the proceedings.

Where the authority of an arbitrator or arbitrators or an umpire is revoked by leave of the court, or where the court removes an umpire who has entered on the reference, or a sole arbitrator or all the arbitrators, the court may, on the application of any party to the arbitration agreement, either

- (a) appoint a person to act as sole arbitrator in the place of the person or persons displaced; or
- (b) order that the arbitration agreement shall cease to have effect with respect to the difference referred<sup>2</sup>.

#### **Powers of arbitrators and umpire :**

The arbitrators or umpire shall, unless a different intention is expressed in the agreement, have power to

- (a) administer oath to the parties and witnesses appearing

<sup>1</sup> Section 6

<sup>2</sup> Section 4

<sup>3</sup> Section 11

<sup>4</sup> Section 12

<sup>5</sup> Section 13.

- (b) state a special case for the opinion of the court on any question of law involved, i.e., refer any question of law arising in course of the arbitration proceeding to the court for the latter's opinion thereon;
- (c) administer to any party to the arbitration such questions as may, in the opinion of the arbitrators or umpire be necessary;
- (d) make an award; this award may be made conditional or in the alternative;
- (e) correct in an award any clerical mistake or error arising from any accidental slip or omission.

#### **Signing and filing of the award :**

When the arbitrators or umpires have made their award, they shall sign it and shall give notice in writing to the parties of the making and signing thereof and of the amount of fees and charges payable in respect of their arbitration and award. The arbitrators must also file the award or a signed copy of it to the court, at the request of any party to the arbitration or at the instance of the court, together with all the depositions and documents which may have been taken or proved before them, upon the payment of all fees and charges due in respect of the arbitration and award and of the costs and charges of filing the award.<sup>1</sup>

#### **Power of court to modify, remit, set aside or confirm the award :**

On the filing of the award the court may—(a) modify or correct the award, or (b) remit the award, or (c) set aside the award, or (d) pronounce judgment in terms of the award.

The court may modify or correct an award in the following cases.<sup>2</sup>

**Power to modify award.** (a) Where it appears that a part of the award is upon a matter not referred to arbitration and such part can be separated from the other part and does not affect the decision on the matter referred; e.g. A and B refer to arbitration a dispute between them regarding the amount of money A owes to B for the latter's construction of a house for A. The arbitrators find in their award the amount of Rs. 4000/-

<sup>1</sup> Section 14 (2)

<sup>2</sup> Section 15

which A owes to B on account of the house. They also find in the award that A owes to B another sum of Rs 5000/- on a separate transaction. Here the arbitrators give an award part of which is upon a matter not referred to arbitration, namely, A's debt to B on the separate transaction. The award thus can be separated into one part which comes within the arbitration and the other part which falls outside. In this case the court may modify the award by striking out the part which falls outside the arbitration or

(b) where the award is imperfect in form or contains an obvious error which can be remedied without affecting such decision, or

(c) where the award contains a clerical mistake or an omission arising from inadvertence or omission

The court may remit or send back the award or any matter referred to arbitration to the arbitrators Power to remit award to recompute for reconsideration upon such terms it thinks fit. The award may be remitted in the following cases<sup>1</sup>

(a) Where the award has left undetermined any of the matters referred to arbitration or where it determines any matter not referred to arbitration and such matter cannot be decided without affecting the determination of the matters referred to arbitration. For example A, B and C are members of a joint family running a business. A asks B and C for an account of past profits alleging that the business is a partnership and not a joint family business. B and C deny the business is a partnership and A's right to an account of past profits. They refer the dispute to arbitration in order to determine whether the business is a partnership or not and whether A has a right to demand an account for past profits. The arbitrators make a award remitting A's right to demand the award but do not decide whether the business is a joint family business or not. Now A's right to an account for past profits is dependent on the business being a partnership for the members of a joint family business cannot demand an account for past profits. So A's right cannot be determined without finding whether the business is a joint family or not.

<sup>1</sup> Section 16

partnership. The court may therefore, remit the award to the arbitrators to determine the nature of the business or

(b) where the award is so indefinite as to be incapable of execution. An award when confirmed by the court is executed like a decree of the court. Therefore it must be sufficiently definite so that the court may execute it. For example A and B two brothers quarrel about the division of properties which their father had left. They refer the dispute to arbitration. The arbitrator makes an award that All properties left by the father north of the Ganges belong to A and all others belong to B. Here the award is indefinite and vague as it does not specify the properties with sufficient clarity so that the award can be executed as decree. The Court may therefore remit the award for more definite ascertainment or

(c) where an objection to the legality of the award is apparent upon the face of it. A lends B money to buy enemy goods. B refuses to repay the money when A demands it. They refer the dispute to arbitration. The arbitrator makes an award ordering B to repay the money. The award is apparently illegal for it is a settled rule of law that the person who lends to another money for an illegal purpose cannot recover the money. The court may therefore reject the award.

Where an award is remitted by the court it must fix the time within which the arbitrator or umpire will submit his decision to the Court but the Court may extend this period subsequently. The award so remitted shall be void if the arbitrator or umpire fails to reconsider it and submit his decision within the time fixed by the Court.

Before the Indian Arbitration Act 1940 came into operation the court could set aside an award if the awards contained setting aside in S 15 Schedule II of the Civil Procedure Code in the ground (1) corruption of an award conduct of the arbitrator or umpire or (2) either party having been guilty of fraudulent concealment of any matter which he ought to have disclosed or of wilfully misleading or deceiving the arbitrator or umpire or (3) the award having been made after the issue of an order by the court superseding the arbitration, or after the expiration of the period allowed by the court, or being otherwise invalid.

But S 20 of the Indian Arbitration Act has wrought changes

in this direction. Under it the Court can set aside an award on one or more of the following grounds.

- (a) That an arbitrator or umpire has misconducted himself or the proceedings. This means that the arbitrator or umpire has shown bias or has taken bribes from one party and so on, or that he has ignored the principles of natural justice, e.g. by carrying on proceedings behind the back of a party without affording him any opportunity to appear and be heard.
- (b) That the award has been made after the issue of an order by the Court superseding the arbitration or after arbitration proceedings have become automatically invalid under S. 35 because of the whole subject-matter of the reference having been referred to regular legal proceedings in a court of law.
- (c) That an award has been improperly procured or is otherwise invalid. This clause is much wider in application than the 2nd clause of S. 15, Schedule II of the Civil Procedure Code as set out above. It not only includes fraudulent concealment of facts or the misleading and deception of the arbitrator or umpire by one party but also any other improper conduct which according to the Court offends the principles of natural justice or is against public policy.

1. Where the court sees no cause to remit the award or any of the matters referred to arbitration for reconsideration or to set aside the award, the court shall, after the time for making

Judgment in terms of the award an application to set aside the award has expired, or such application having been made, after refusing it, proceed to pronounce judgment according to the award, and upon the judgment so pronounced a decree shall follow, and no appeal shall lie from such decree except on the ground that it is in excess of, or not otherwise in accordance with, the award.<sup>2</sup>

#### **Effect of submission or reference to arbitration :**

When any person enters into an agreement with another to refer all disputes between them, either existing or future, to

<sup>2</sup> Section 17.

arbitration, he cannot institute any suit in a court of law relating to those disputes, otherwise the very purpose of arbitration will be frustrated.

If he institutes any such proceedings against the other party, the latter can apply to the court before which the proceedings are pending, to stay the proceedings and the court will grant in order staying such suit or proceeding provided the following conditions are satisfied<sup>1</sup>:

(1) That the suit or proceeding is in respect of the matter agreed to be referred to arbitration. Before an order can be made for stay of the suit the court must be satisfied that the suit has been instituted in respect of a matter agreed to be referred. If the subject matter of the suit falls outside the scope of the submission the court will not stay the suit<sup>2</sup>. If, however, the suit relates to matters which lie partly within the submission and partly not covered by the submission it depends on the discretion of the court to grant a stay order or not. In such case it is not right to cut up the litigation into two portions one to be tried by the court and the other by arbitration<sup>3</sup>.

(2) That the applicant was and still remains ready and willing to do all things necessary for the proper conduct of the arbitration.

(3) That there is no sufficient reason why the matter could not be referred in accordance with the arbitration agreement.

(4) That the party instituting the suit was not induced to file the arbitration agreement by fraud.

(5) That the party filing the suit did not file a written statement by way of defence in the suit, so as to be tried or taken any other step in the proceeding. The following have been held to be steps in the proceeding which render a defendant to a suit from a position to try and to the strength of an arbitration agreement:

(i) An application for stay of suit coupled with an order for security from the plaintiff.

<sup>1</sup> Section 34.

<sup>2</sup> *cf. Jnanendra vs Sinclair Murray & Co.* 34 C.I.J. 173.

<sup>3</sup> *Thomas vs Port Sea S S Co* (1912) A.C. 1.

<sup>4</sup> *Turnock vs Sartoris*, 43 Ch.D. 150.

<sup>5</sup> *Adam vs Cattey*, (1892) 66 L.T. 68.

- (b) An application for further time to file the writer statement<sup>1</sup>
- (c) An application for leave to administer interrogatories *i.e.* questions to the other party
- (d) Appearance without objection on a Chamber Summon to give directions
- (e) Submitting to the jurisdiction of the Court<sup>2</sup>

If the court is satisfied that the matter should be decided by arbitration, it stays the suit or proceeding. It does not dismiss the suit for in case the award is remitted or set aside the stayed suit can be heard without the necessity of instituting it all over again.

#### **Arbitration through the intervention of the court:**

This occurs in two cases (1) where there is no suit pending or (2) where there is a suit.

Where two or more parties have agreed to refer to arbitration their future differences before the institution of Arbitration may suit and such differences have actually through court arisen they can one of them instead of proceeding with the arbitration forthwith is allow is pending may apply to the court that the arbitration agreement be filed in court.

On such application being made the Court shall direct that thereon to be given to all parties to the agreement also the application requiring that the same with arbitration be filed in the court why the court should not do so.

Where no sufficient cause is shown the Court shall direct the application to be filed immediately in order of service to the other party by the parties whereby the court is not or cannot be approached directly by the parties.

W <sup>1</sup>	W <sup>2</sup>	W <sup>3</sup>	W <sup>4</sup>
Mr <sup>1</sup>	Mr <sup>2</sup>	Mr <sup>3</sup>	Mr <sup>4</sup>

<sup>1</sup> *S. H. Bonner vs The Corporation of Calcutta* 21 Cal 443, 11 CWN 306  
<sup>2</sup> *K. Ram Industrial Park Ltd vs Satya Narain* 29 CWN 771

<sup>3</sup> *Chippel vs North* (1891) 7 O.B. 257

<sup>4</sup> *County Theatres and Hotel vs Knowles* (1902) 1 K.B. 499

<sup>5</sup> *Khardar vs Rukmanand* 2 A.I.T. 775

<sup>6</sup> Section 20

**Arbitration in suits.** to arbitration, they may at any time before judgment is pronounced apply in writing to the Court for an order of reference.<sup>1</sup> On such an application the

Court will appoint an arbitrator in such manner as may be agreed upon between the parties. The Court will also refer to the arbitrator the matter in difference which he is required to determine, and shall in order specify such time as it thinks reasonable for the making of the award.<sup>2</sup>

Where *some* only of the parties to a suit apply to have the matters in difference between them referred to arbitration in accordance with, and in the manner provided by Sec. 21 as above, the Court may, if it thinks fit, so refer such matters to arbitration (provided that the same can be separated from the rest of the subject-matter of the suit) in the manner provided in that section. But the suit shall continue so far as it relates to the parties who have not joined in the said application and to matters not contained in the said reference as if no such application has been made, and an award made in pursuance of such a reference shall be binding only on the parties who have joined in the application.<sup>3</sup>

### **Statutory Arbitration :**

Arbitration is enjoined by certain statutes. For example, the Co-operative Societies Act lays down that certain disputes between a member and a Co-operative Society must be settled by arbitration and not by suit. This type of arbitration is known as Statutory Arbitration and the procedure relating to such arbitration is mostly laid down by the Acts which enjoin such arbitration. But in so far as the Acts are silent about certain points regarding such proceedings the provisions of the Indian

<sup>1</sup> Section 21.

<sup>2</sup> Section 23.

<sup>3</sup> Section 24.

## CHAPTER VIII

### INSURANCE

There is no statute relating to insurance law in India. The Insurance Act (IV of 1938) deals only with the constitution, management, regulation and control of insurance companies. It does not embody any law of the contract of insurance. The English law relating to insurance is, therefore, applied and followed in India subject to the provisions of the Indian Contract Act. Thus the capacity of parties for entering into a contract of insurance is governed by the Indian Contract Act and not the English law.

#### **The Contract of Insurance :**

"The aim of all insurance is to make provisions against dangers which beset human life and dealings. Those who seek it endeavour to avert disaster from themselves by shifting possible losses on to the shoulders of others, who are willing, for pecuniary consideration, to take risk thereof, and in case of life assurance, they endeavour to assure to those dependent on them a certain provision in case of their death, or to provide a fund out of which their creditors can be satisfied."<sup>1</sup> A contract of insurance is the result of a historical process whereby civilised man has found a device by means of which he can keep himself protected from contingencies which are uncertain in their incidence e.g. fire or theft or from contingencies which are certain but the time for the happening of which is uncertain e.g. death. The most admirable definition and the exposition of the nature of a contract of insurance is to be found in the judgement of Channel J. in Prudential Insurance Co. v. Inland Revenue<sup>2</sup>. The observation of the learned judge is as follows : "Where you insure a ship or a house you cannot insure that the ship will not be lost or the house burnt, but what you do insure is that a sum of money shall be paid upon the happening of a certain event. That I think is the first requirement in a contract of insurance. It must be a contract whereby for some consideration, usually but not neces-

<sup>1</sup> Porter's Law of Insurance, p. 1.

<sup>2</sup> (1904) 2 K.B. 658, 663.

sarily periodical payments called premiums, you secure to yourself some benefit, usually but not necessarily the payment of a sum of money, upon the happening of some event. Then the next thing that is necessary is that the event should be one which involves some amount of uncertainty. There must be either uncertainty whether the event will ever happen or not, or if the event is one which must happen at some time there must be uncertainty as to the time at which it will happen. The remaining essential is that . . . the insurance must be against something. A contract which could otherwise be a mere wager may become an insurance by reason of the assured having an interest in the subject-matter, that is to say, the uncertain event which is necessary to make the contract amount to an insurance must be an event which is *prima facie* adverse to the interest of the assured. The insurance is to provide for the payment of a sum of money to meet a loss or detriment which will or may be suffered upon the happening of the event. By statute it is necessary that at the time of making of the contract there should be an insurable interest in the assured. It is true that in the case of life insurance it is not necessary that the interest should continue and the interest should be the measure of the amount recoverable as in the case of a fire or marine policy. Still the necessity of there being an insurable interest at the time of making the contract shows that it is essential to the idea of a contract of insurance that these events upon which the money is to be paid shall *prima facie* be an adverse event." A contract of insurance, then, must be, in the words of Channel J., a contract for the payment of a sum of money, or for some corresponding benefit such as the rebuilding of a house or the repairing of a ship, for some consideration usually but not necessarily for periodical payments called premiums, to become due on the happening of an event which event must have some amount of uncertainty about it and must be of a character more or less adverse to the interest of the person effecting the insurance.

A contract of insurance is usually contained in a document which is called the 'policy.' The party who undertakes the risk and the liability to indemnify is called the 'insurer' and having subscribed the policy, the 'underwriter.' The party who is indemnified is called the 'insured' or 'assured'.

#### **Insurance and Assurance :**

Historically "assurance" is an earlier term and the term

'insurance' is of recent origin. Until the end of the sixteenth century, the term assurance was used to designate all types of insurance e.g. marine, fire or life. But subsequently, the term assurance came to designate life insurance only and the term insurance came to be applied to marine and other miscellaneous insurance business. The distinction seems to have been based on the principle that the risk insured must in respect of life policies be a certain event and is such the term assurance should properly be applied to them. It should be noted, however, that the distinction is hardly observed now days and the word insurance is used in a synonymous and not a distinctive manner.

### **Contract of Insurance is a Contract of Indemnity :**

A contract by which one party binds over another for the other from loss due to any particular chance is called a contract of indemnity. Contract of insurance are of two kinds i.e. those which regard those which are not in the nature of contract of indemnity. E.g. marine and other insurances of property and personal of nature are proper contracts of indemnity. In the case of the usual loss entitling to recover from the insurer the actual loss suffered owing to the peril insured against and not more, "more or less".<sup>1</sup> Lord Esher observed in *Costello v. Preston*, "The contract of insurance contained in a marine or fire policy is a contract of indemnity and of indemnity only, and that is to say means that the assured, in case of loss against which the policy has been made, shall be fully indemnified, but shall never be more than fully indemnified. That is fundamental principle of insurance and if ever a proposition is brought forward which is at variance with it that is to say, which other will prevent the assured from obtaining a full indemnity or which will give to the assured more than full indemnity, the proposition must certainly be wrong".

**Life Assurance, Personal Accident Assurance, Health Assurance and Burglary Assurance** are not, however, contracts of indemnity. In these cases the assured gets the stipulated amount on the happening of the event insured against, irrespective of the actual pecuniary loss suffered.

### **Insurance Contract, a contract Uberrima Fidei :**

We have seen before that an ordinary contract of agency must satisfy the test for himself<sup>1</sup>. This is not necessary if the agent is obliged to disclose all facts known to him in the course of his trade which may affect the interest of the principal. Uberrima Fidei is a very useful word which indicates that influence or knowledge of the agent must not be exercised by him except in the way he is lawfully entitled to do so.

The test of disclosure in insurance is that the agent should truthfully advise the insured of all facts which may affect the proposed insurance which could possibly damage the insured. It is not necessary to disclose the name of the person who influenced the agent to take up the policy. Any influence exerted under the name of the insured will not be considered to be undue disclosure of facts which should not be

disclosed which will affect the proposed contract. The agent need not disclose facts which are not known to him and yet claim him to be ignorant and innocent. It is also not necessary to disclose facts which are properly immune from disclosure. Careless operation disclosed to an insurer will constitute such a fact if it is required to void the contract. As a rule the law of disclosure to be decided in very conflict. The test can be to decide if the matters concealed and concealed had been duly disclosed they would not make a difference in the evidence have influenced reasonable insurer to decline the risk or to quote a higher premium.

The duty to disclose is only with regard to the complete contract. Any fact occurring or coming to the knowledge of the assured after the contract need not be disclosed.

<sup>1</sup> See supra, Law of Contract and Civilian Empor.  
Life Assurance of Scotland vs Foster 4 Bing Life and Accident  
Insurance cases, 520

<sup>2</sup> Mutual Life Assurance vs Ontario Metal Products, (1935) A.C. 344

In the absence of inquiry by the insurer the following circumstances need not be disclosed by the assured :—

- (a) Any circumstance which diminishes the risk;
- (b) Any circumstance which is known or presumed to be known to the insurer. The insurer is presumed to know matters of common notoriety or knowledge, and matters which an insurer in the ordinary course of his business as such, ought to know;
- (c) Any circumstance as to which information is waived by the insurer;
- (d) Any circumstance which is superfluous to disclose by reason of any express or implied warranty.

In certain cases where the validity of a contract of insurance is conditional upon the truth of the statement made, a policy will be void by reason only of an inadvertent and immaterial misstatement and the materiality of the statement will not be of any importance.

#### **Contract of Insurance and Wager :**

In *Wilson vs. Jones*<sup>1</sup> Willes J. observed, "The distinction between a wagering contract and one which is not a wager depends upon whether the person making it has or has not an interest in the subject-matter of the contract." Applying this test it becomes absolutely clear that a policy of insurance cannot be regarded as a wagering contract. A policy is, properly speaking, in the words of Blackburn J.<sup>2</sup>, a contract to indemnify the insured in respect of some interest which he has against the perils which he contemplates it will be liable to. But in a wagering contract which relates to betting upon a future event, the parties to it do not contemplate of covering any risk or indemnifying any loss in respect of any interest or property; for the parties have no interest in the subject-matter of the contract apart from that created by the contract itself. As Porter says<sup>3</sup>, " in a pure wager the interest of the contracting parties in the event wagered on is created by the fact that they have to pay each other certain sums in certain event, but that neither sum is due until the event has been decided one way or other:

<sup>1</sup> L.R. 2 Ex. 141.

<sup>2</sup> *Wilson vs. Jones*, Ibid.

<sup>3</sup> *Porter's Law of Insurance*, pp. 45.

whereas in insurance the motive for the contract springs from the existence of something which may be lost, and the danger of loss thereby to the person who seeks insurance. Such person pays, and not merely risks money to obtain security against possible loss.'

### **Insurable Interest :**

We have already seen that an insurance contract differs from a wager because the assured has an interest in the subject-matter which he endeavours to protect from the perils insured against. It follows from this that no contract of insurance is valid unless the assured has some interest in the subject matter at the time of the contract. Thus if A insures a ship or a house belonging to B and in which he has no interest whatsoever, the contract is void and the insurer is not bound to indemnify him in case of loss. The interest which the assured possesses in the subject matter in a contract of insurance is known as "insurable interest". In considering the question of insurable interest says Macgillivray<sup>1</sup>:

"It is necessary at the outset of the inquiry to distinguish between the interest which the law requires the assured to have in the subject matter of insurance and the interest which is required by the terms of particular contract under consideration. An interest is required by the terms of contract itself if the promise of the insurer is merely to indemnify the assured against pecuniary loss arising from the event insured against. If the assured has no interest at the time the event happens, it is clear that he cannot recover anything, because he suffers no damage and has therefore no claim to an indemnity. Similarly if he has an interest which is limited to something less than the full value of the subject matter he suffers no greater damage than the value of his interest at the time of loss, and therefore his claim to indemnity cannot exceed the value of his interest. It should be noted, however, that only in contracts of indemnity e.g. fire or marine insurance is any interest required by the terms of the contract. In insurance contracts, e.g. life or accident insurance, which are not contracts of indemnity, no interest is required by the terms of the contract. But even in these cases the law requires

<sup>1</sup> Macgillivray's Insurance Law 2nd ed p 184

<sup>2</sup> E.g. when the assured sells his ship or house insured prior to the date when the loss occurs

the assured to have some interest in the subject matter, otherwise the contract would be void as a wager. Thus a man cannot put out an insurance on the life of a total stranger nor on that of one who is not so connected with him as to make the continuance of the life a matter of some real interest to him. It is now well settled that a man has no insurable interest in his own life and in that of his wife and children. Indeed any reasonable expectation of pecuniary benefit will always "strip it of its interest" and another create an insurable interest in such life.

### **Re-insurance :**

When an insured or underwriter thinks that he has undertaken too big a risk or liability he can have part of the risk re-insured with another insurer. A re-insurer is thus a person by whom, in consideration of a certain premium, the original insurer throws upon either the risk for which he is liable himself responsible or by whom it is assured, to whom however he alone is liable in the original insurance. A re-insurance contract does not supersede the original insurance contract. The original insured cannot limit his amount from the re-insurer until the original insurer still remains liable to be indemnified. The only consequence of a re-insurance contract is that if the original insured recovers the claim insured can from the general insurer, the latter can recover a part of it which he has insured with the re-insurer. For example A owns his shop worth B for Rs. 50,000/- He thinks the liability too great and re-insures half the risk with C for Rs. 25,000/- If the shop is lost A cannot recover any money from B but he can recover Rs. 50,000/- from B. B, of course by virtue of the re-insurance can claim half the sum i.e. Rs. 25,000/- from C.

### **Double Insurance :**

If a person insure the same property with more than one insurer, the insured is said to effect a double insurance. If he effects a double insurance *without any fraudulent intent* he can recover on all the policies, provided the total value of all the policies does not exceed the actual value of the property insured. If, however, the total value of the policies exceeds the actual value of the property, he can recover only the actual value.

<sup>1</sup> Arnold on Marine Insurance

He may recover the whole of his actual loss from one insurer, in which case the other insurers must contribute proportionately to the first insurer. He may also recover as much as he has paid under one policy and if that does not satisfy his loss he may recover from the other policies. In this case no single insurer will bear more than a proportionate share of loss the other insurers having a liability convertible contribution to the first insurer.

### Different Types of Insurance :

The most common types of insurance contracts are the following:

- (1) Marine Insurance
- (2) Fire Insurance
- (3) Life Insurance
- (4) Personal Accident Insurance
- (5) Insurance on Fidelity
- (6) Guarantee Insurance

We shall discuss some of these shortly.

### Marine Insurance :

In England there is no statute of its own, covered by the Marine Insurance Act 1906, but the Act of Parliament does not embody all the principles of marine insurance which have been developed by English Courts from time to time. In interpreting the law relating to marine insurance reference is therefore frequently made to the law existing at the time of the passing of the Act. In India we have no statute dealing with marine insurance and the Marine Insurance Act 1906 is not applicable to India. But the principles of English law as embodied in English and Indian Law as also in the Marine Insurance Act 1906 are applicable to and govern marine insurance in India.

### Nature and Definition of Marine Insurance :

A contract of marine insurance is a contract whereby the insurer undertakes to indemnify the insured in manner and to the extent thereby agreed against marine losses that is to say, losses incident to marine adventure.<sup>1</sup> Marine insurance is there-

<sup>1</sup> Marine Insurance Act, 1906, S. 1

fore, a contract of indemnity. The document in which the contract of marine insurance is generally embodied is called a *policy*. The insurer as soon as he subscribes his name to the policy is called the *underwriter*. The thing or property insured is called the subject-matter of insurance. The interest which the assured has in the subject-matter is known as his insurable interest. The payment in consideration of which the insurer undertakes to indemnify the assured is termed the *premium*. The risk which the assured insures against is the loss which may be occasioned by maritime perils and casualties.

### **Requisites of a valid Marine Insurance Policy :**

By S. 22 of the Marine Insurance Act, a marine insurance contract in England is invalid and inadmissible in evidence unless it is embodied in a marine policy and signed by or on behalf of the insurer specifying (a) the name of the assured or some person who effects the insurance on his behalf; (b) the subject-matter insured and the risk insured against; (c) the voyage or period of time or both, as the case may be, covered by the insurance; (d) the sum or sums insured; (e) the name or names of the insurers.

In India the only statutory requirements for a valid contract of marine insurance are contained in S. 7 of the Indian Stamp Act, 1899, which are as follows :

- (a) No contract of sea-insurance (other than such insurance as is referred to in section 506 of the Merchant Shipping Act, 1894), shall be valid unless the same is expressed in a sea-policy.
- (b) No Sea policy made for time shall be made for any time exceeding twelve months.
- (c) No Sea policy shall be valid unless it specifies the particular risk or adventure, or the time, for which it is made, the names of the subscribers or underwriters, and the amount or amounts insured.

But in India marine insurance contracts, by practice, specify the particulars required by English law over and above those required by the Indian Stamp Act.

A marine insurance policy must also be duly stamped both in England and India.

### **Subject-matter of Insurance and the risks insured against :**

Usually marine insurances are mostly on ships or goods, freight or profits. But every lawful maritime adventure may be the subject of a contract of marine insurance and according to the Marine Insurance Act, there is a marine adventure wherever any ship, goods or other moveables are exposed to maritime perils. We shall discuss later as to what are maritime perils.

### **Contract how made :**

A contract of marine insurance is effected, as in the case of every contract by offer and acceptance—the offer of the assured as accepted by the insurers and underwriters. The offer of the assured is usually communicated by an insurance broker who, on receiving instructions from the assured as to the nature of the risk and the rate of premium at which the insurance is to be effected, prepares what is commonly known as a "slip", containing rough notes indicating the terms of the proposed insurance. The broker then takes the slip round to the various underwriters, who may be private Lloyd's underwriters or underwriters on behalf of corporations. Those underwriters, who are willing to accept the risk, do so by initialing the slip for the amounts for which they are willing to become insurers. If the underwriters who accept are Lloyd's underwriters, the broker prepares a policy for them to which they subscribe. But insurance companies prepare their own policies.

The insurance slip forms the concluded contract and once accepted neither party can resile from it without committing breach of contract. Though it is the contract, the assured cannot sue the insurer unless a proper policy is issued fulfilling the requirements of the statute and the Stamp Act in England and the Stamp Act in India<sup>1</sup>. But once the slip is accepted an action may be maintained by the assured to issue a policy and specific performance of it may be ordered<sup>2</sup>.

### **Lloyd's Policy :**

The ordinary form of a policy of marine insurance which is almost universally used in England and India is what is known in the insurance world as "Lloyds policy".

<sup>1</sup> Surjinaull *vs.* Triton Insurance Co., 29 C.W.N. 893 p.c.=52 Cal. 408.

<sup>2</sup> Bhagwanlal *vs.* Netherlands India Sea and Fire Insurance Co. of Batavia, (1888) 14 A.C. 83, p.c.

In policies on ships a clause known as the running down or collision clause is generally incorporated.

The principal parts of the policy are—

- (1) the name of the insured or his agent
- (2) the name of the ship
- (3) the subject-matter of insurance
- (4) the voyage insured
- (5) the perils insured against
- (6) the date and subscription
- (7) the valuation
- (8) the sue and labour clause
- (9) the common memorandum
- (10) the running down clause
- (11) the stamp
- (12) Warranties

We shall discuss each of these clauses separately.

#### **/ Name of the insured :**

A marine policy in England must specify and in India by practice specifies, as we have already seen, the name of the assured or some person who effects the insurance on his behalf. A Lloyds policy may be effected in the name either of the assured, or of the broker, or of an agent and the action on the policy may be instituted either in the name of the assured or in that of such broker or agent.

#### **2 Name of the ship :**

The identity of insured goods is very important in marine insurance since the insurers are liable to indemnify for the loss of insured goods only. It is, therefore, necessary that the name of the ship in which the insured goods are carried must generally be specified. As the name of the ship is specified only for the purpose of identifying her, a misstatement of the name will not discharge the liability of the underwriter if it is proved that the underwriters in fact intended the policy to cover the ship on which the loss actually occurred. It is, therefore, common to insert a

clause in the policy "or by whatsoever other name or names the ship may be called," the effect of which is to render a mistake in the name immaterial if the identity of the ship can be proved and the under-writer be not prejudiced by it.

### Floating Policies :

Where the assured does not know on what ship or ships the insured goods have been or may be loaded, he may effect an insurance of the goods without specifying the ship or ships. In such a case the policy is known as a floating policy. A floating policy has been defined<sup>1</sup> as a policy which describes the insurance in general terms and leaves the name of the ship or ships and other particulars to be defined by subsequent declaration. A floating policy on goods "on board ship or ships" covers goods loaded at any port within the limits of the insured voyage.<sup>2</sup>

### Subject-matter of Insurance :

The subject-matter insured must be specified with reasonable certainty in a marine policy. Where the subject-matter is the ship it is usual to insert either at the foot or the margin of the policy the words "on ship" or by stating the same in the valuation clause. The word includes the hull, the machinery, the boilers, all the fittings, the stores and provisions for the crew and the staff and engine stores. The term goods means merchandise and does not include personal effects belonging to the master or passengers.

The following interests must be specifically insured and are not included in the denomination of goods or ship :—

- (a) freight—freight includes not only money payable to the ship owner for the carriage of goods, but also any benefit derived by him from the employment of the ship, such as money paid by the charterer for the hire of the ship, or the benefit derived by the ship-owner by the carriage of his own goods. This is not included in the general term of goods on ship.
- (b) profits, which means expected profits which a purchaser of goods-to-arrive would make if the goods arrived safely, are not also included in the term goods on ship.

<sup>1</sup> Marine Insurance Act, 1906, s. 29.

<sup>2</sup> *Hector v. Leathley* (1830) 10 B. & C., 858.

(c) Deck cargoes and living animals in the absence of a usage to the contrary.

### The Voyage or Duration of Risk :

Where the contract is to insure the subject matter for a fixed period of time the policy is called a "time policy". Where, however, the contract is to insure the subject matter at and from or from one place to another or others, the policy is called a "Voyage policy". Time policy is generally effected on ships and freight and voyage policy on goods.

### Time Policy :

The two limits of the time mentioned in a time policy determine the period during which the insurer remains liable to indemnify the assured or, in other words, the insured period. The assured is entitled to be indemnified for any loss occurring during this period and the insurer is, in his turn, entitled to the full payment of the premium stipulated.

"A time policy, however, may be effected retrospectively by the insertion of the ordinary clause 'lost or not lost'; for instance, if a policy is effected on 15th August, 1911, to commence on the 1st day of the same month, it will cover any losses occurring after the latter date"<sup>1</sup>

Where a time policy expresses to commence from a certain day and continues until another day, the risk does not commence unless otherwise provided, until the former day has expired and will continue until the expiration of the latter day.

### Voyage Policy :

In a voyage policy where the subject matter is insured "at" a particular place the risk does not attach until the ship starts on the voyage insured.<sup>2</sup> Where the subject matter is insured "at and from" a particular place, and the ship is at that place in good safety when the contract is concluded, the risk attaches immediately.<sup>3</sup> If the ship be not at that place when the contract is concluded, the risk attaches as soon as she arrives there in good safety.

<sup>1</sup> Halsbury's Laws of England, Vol. XVII, p. 381

<sup>2</sup> Marine Insurance Act, Sch. I, r. 2.

<sup>3</sup> Marine Insurance Act, Sch. I, r. 3.

In a voyage policy where the insurance is 'at and from' or 'from' a particular place, it is not necessary that the ship should commence at that place at the time of the contract. But within a reasonable time there is an implied undertaking by the assured that the ship should commence the insured voyage within a reasonable time. A reasonable time must be allowed for the ship to prepare and undertake the adventure and what is a reasonable time must be decided not by any positive or arbitrary rule but by the state of things in the port where the vessel happens to be.<sup>1</sup> If the ship fails to come to the port where the insured risk was to commence or undertake the voyage within a reasonable time so as to materially alter the risk for instance to change summer risk into winter risk the contract is voidable at the instance of the insurer. But this implied undertaking may be negatived by showing that the delay was caused by circumstances known by the insurer before the contract was concluded or by showing that he waived the condition.

In a voyage policy the port of departure is generally specified. Alteration of the port of departure instead of sailing from the specified port if the ship sails from any other port the risk does not attach and the insurer is not liable for any loss. The place of departure is called *terminus a quo* and the place of destination is called *terminus ad quem*.

A deviation from the proper course of the insured voyage Deviations and change of course from what is known is (a) a change of voyage and (b) deviation. The distinction between the two should be noted.

A change of voyage takes place when the destination of the ship is voluntarily changed from that contemplated by the policy. The insurer is discharged from liability as from the time when the intention to change is manifest and it is immaterial that the ship may not in fact have left the course of voyage contemplated by the policy when the loss occurs.

Deviation takes place (1) where the course of the voyage is designated by the policy and that course is departed from

<sup>1</sup> Raymond, (1893) A.C. 22, 32  
Time Insurance Co. v. Stearns, (1901) 2 K.B. 912  
Insurance Act 1906, S. 42  
Insurance Act 1906 Ss. 43, 44 and 45  
S. 45

or (2) where the course of voyage is not specially designated by the policy, but the usual and customary course is departed from.<sup>1</sup> In the absence of any stipulation in the policy for any voyage, the ship is bound to proceed from one terminus to the other of the insured voyage in a direct course and without touching at any interjacent port or pursuing any intermediate adventure.

Where a ship, without lawful excuse, deviates from the voyage contemplated by the policy, the insurer is discharged from liability as from the time of deviation; and it is immaterial that the ship may have regained her route before any loss occurs<sup>2</sup>. In the case of deviation the insurer is discharged not from the moment when the intention to deviate is apparent but from the moment when deviation in fact takes place.

The eighth clause in a Lloyds' policy allowing liberty to the ship "to proceed and sail to, and touch and stay at any port or place whatsoever" does not authorise the ship to depart from the direct course of her voyage from one terminus to the other of the insured voyage or to visit any port for any purpose unconnected with the main object of the adventure.<sup>3</sup> This is also generally true even when there is a clause giving liberty "to touch and stay at any place for all purposes whatsoever."

In a voyage policy there is also an implied condition that the Delay in adventure insured shall be prosecuted throughout voyage its course with reasonable despatch, and, if without lawful excuse it is not so prosecuted, the insurer is discharged from the time when the delay became unreasonable.<sup>4</sup> It seems that delay will be held to become unreasonable when the nature of the risk insured against becomes different as when summer risk is changed into winter risk due to the delay.

**Excuse for deviation** Deviation or delay in prosecuting the voyage or delay contemplated by the policy is excusable —

- (a) Where authorised by any special item in the policy; or
- (b) Where caused by circumstances beyond the control of the master and his employer; or

<sup>1</sup> Marine Insurance Act, S. 46

<sup>2</sup> Ibid, S. 46 (1)

<sup>3</sup> Marine Insurance Act, 1906, Sch 1, Laughorn (1812) 4 Taunt 511.

<sup>4</sup> Marine Insurance Act, 1906, S. 49 (1)

- (c) Where reasonably necessary in order to comply with an express or implied warranty, or
- (d) Where reasonably necessary for the safety of the ship or the subject matter insured, or
- (e) For the purpose of saving human life, or aiding a ship in distress where human life may be in danger, or
- (f) Where reasonably necessary for the purpose of obtaining medical or surgical aid for any person on board the ship, or
- (g) Where caused by the tortious conduct of the master or the crew but may be one of the perils insured

### **Perils :<sup>1</sup>**

Clause II in a marine insurance contract states the following perils which are mentioned again in all English policies contain the same words. "The sum of £ 1000 of the seas, men of war, his enemies' ships, or the captures, letters of marit and countermand suspensions taken, if sea arrests, restraints and detenments of all kings, princes and people, of what nation, condition or quality soever, hostility of the master and mariners, and of all other perils losses and misfortunes that have or shall come to the hurt detriment or damage of the said . . . , or any part thereof" We shall discuss these perils separately.

### **Perils of the Seas :**

The term "perils of the sea" does not lend itself to an easy definition. It does not include any casualty which may happen to the subject matter of insurance on the sea. It must be as Lord Herschell observed in the *King/o* "a peril of the sea, as well as a peril on the sea." Thus if the subject matter be the ship it does not cover any loss due to the ordinary wear and tear or any injury to machinery or engine, due to the bursting of the air chamber of a donkey, engine owing to a very heavy cloud or due to the ship being unseaworthy at the time of the contract. If the subject matter be goods, it will not cover any damage arising solely from corruption of the subject matter as when fruit becomes rotten or deteriorates due to the process of nature and not from external

<sup>1</sup> Marine Insurance Act 1906, S 49 (1)

<sup>2</sup> (1887), 12 A.C. at p 509

cause or from death or destruction of the subject matter as when living animals die from natural causes or loss is caused by rats, insects or other vermin. The insurers will only be liable if the damage or loss is the proximate result of some fortuitous accident of the sea e.g., action of the wind and waves. The Marine Insurance Act, 1906,<sup>1</sup> therefore, lays down that the term 'perils of the seas' refers only to fortuitous accidents or casualties of the sea, and does not include the or huius action of the winds and waves.

#### **Fire :**

Loss by fire covers fire caused by any common accident e.g. lightning or by the enemy or by the ship being burnt in order to prevent capture or from an apprehension of a contagious disease on the like and also loss due to steps taken in order to prevent a fire.

#### **Enemy :**

Loss due to the capture by the enemy in times of war is covered by this clause.

#### **Pirates, Rovers and Thieves :**

This clause covers loss due to the action of pirates, rovers and thieves. Pirates include passengers who mutiny and rioters who attack from shore. The term thieves does not cover secret thefts by the crew or passengers. But robbery with violence by strangers is a loss by rovers or thieves.

#### **Jettison :**

This clause covers loss due to the throwing of goods over board in order to prevent capture by the enemy.

#### **Takings at Sea, Arrests, Restraints, Detainments of King, Princes and People :**

Taking at sea includes both capture by the enemy and seizures as by revenue or sanitary officers of a foreign state. Arrests, restraints etc., refer to loss owing to political or executive acts of foreign ruling powers and do not include loss by riot or by ordinary judicial process.

<sup>1</sup> Sch. I, r. 7.

### **Bartistry :**

Bartistry is derived from an Italian word which means to cheat. This clause covers all loss due to the wrongful acts wilfully committed by the master or crew of the ship, to the prejudice of the owners or charterers which are called bartistry. Sailing out of port without paying port dues or in breach of an embargo, or wilful breach of blockade whereby the ship is seized or other loss is sustained or deviation in fraud of the owner, may amount to bartistry.

### **Other Perils :**

The general words we intend to cover risks similar to those enumerated above but which do not fall within any of those. In *Cullen vs Butter*<sup>1</sup> the words came before the court for construction. In that case the ship insured was fired upon and sunk by the crew of another British ship in the mistaken belief that the former was an enemy ship. It was held that though the cause was not perils per se of the seas yet it came within the general words "all other perils etc."

### **Date and Subscription : 4**

By this clause each under writer separately acknowledges the receipt of the premium and also binds himself severally and jointly to indemnify the assured to the extent of this subscription in case of loss.

### **Valuation Clause : 7**

As we have already seen, a Lloyds policy contains the following clause - the said ship etc goods and merchandise etc, for so much as concerns the assured by agreement between the assured and insurers in this policy we and shall be valued at. If the clause is to value is not filled up, the policy is known as *unvalued or open policy*. If it is filled up it becomes a *valued policy*. The difference in legal effect between the two policies is that in the case of an unvalued policy the value of the subject matter is not agreed upon but has to be ascertained subsequently in case of loss, whereas in the case of a valued policy the value

fixed in the policy is conclusive unless it is voidable on the ground of fraud.

### Suing and Labouring Clause : 8

This clause means that if the assured or his agent incurs expenses by employing labour or otherwise for preventing a loss for which the insurer would be answerable, the insurer is liable to contribute proportionately towards the expenses incurred by the assured though such expenditure is not strictly speaking a loss due to the perils insured against.

### Memorandum : 9

The memorandum states that the insurer is not liable to make good any partial loss on corn, fish, salt, fruit, flour, and seed and to make good any partial loss under five or three per cent., the other classes of goods specified. But the insurer remains liable in the case of general average loss or the ship being stranded. The purpose of the memorandum is to get rid of the difficulty of discriminating between small losses by perils at the sea and those caused by wear and tear or deterioration and to prevent disputes about trifling matters.

### Stamp : 10

We have already seen that a valid marine policy must be duly stamped.

### Warranties : 11

A marine policy usually contains warranties by the assured. Certain warranties are expressly provided either in the body or margin or at the bottom of the policy. These are called express warranties. Over and above these certain warranties are implied by law. These are called implied warranties. A warranty, as defined by the Marine Insurance Act, 1961<sup>1</sup>, means a promissory warranty, that is to say, a warranty by which the assured undertakes that some particular thing shall or shall not be done or that some condition shall be fulfilled, or whereby he affirms or negatives the existence of a particular state of facts.

A warranty is a condition which must be exactly complied

<sup>1</sup> S. 33 (1)

with, whether it be material to the risk or not. If it be not so complied with, then subject to any express provision in the policy, the insurer is discharged from liability as from the date of the breach of warranty, but without in any way affecting his liability, if any, incurred by him before that date.<sup>1</sup>

#### **Non-Compliance with a warranty is excused—**

- (a) When by reason of a change of circumstances the warranty ceases to be applicable, as when the warranty to sail in convoy becomes inapplicable on the cessation of hostilities, or when the warranty is rendered unlawful by any subsequent law.
- (b) When the breach of warranty is waived by the insurer.

#### **Express Warranties :**

The most common express warranties are with reference to the following —

- (a) The time of sailing. A warranty that a ship will sail or has sailed on a particular day means that she shall be or was on her voyage on that day. Merely that she had her cargo on board or that she was prevented from sailing by stress of weather would not amount to a compliance of the warranty.
- (b) The safety of the ship at a particular time.
- (c) The limits of the vessel's navigation. In time policies warranties prohibiting the ship from certain hazardous and risky localities either altogether or at certain times, are frequently inserted in order to reduce the risks of the insurer. If the ship enters the prohibited zone at the prohibited time and loss accrues the insurer is discharged of liability. Thus where a ship was not allowed by the policy to enter the Gulf of St. Lawrence before a certain date, nor to be in the gulf after a certain date and was lost while in the gulf after the

<sup>1</sup> Marine Insurance Act, 1906, S. 33 (3).

<sup>2</sup> Ibid, S. 34

prohibited date, the insurers were held not liable for the loss<sup>1</sup>.

- (d) To depart with convoy—This is usually warranty inserted in times of war with a view to protect the insurer from the hazards of enemy action.
- (e) The neutrality of the property—This warranty is also inserted in times of war in order to protect the insurer from the risk of the insured property being seized as enemy property.

#### **Implied Warranties :**

The implied warranties in a voyage policy are the following :—

- (a) Not to deviate—We have already seen what is deviation and how deviation discharges the liability of the insurer.
- (b) Seaworthiness—In a voyage policy there is an implied warranty that at the commencement of the voyage the ship shall be seaworthy for the purpose of the adventure insured. But there is no warranty that the ship shall continue to be such until the termination of the voyage. There is also no such warranty in the case of time policies<sup>2</sup>.

In the case of every kind of policy there is an implied warranty that—

- (a) The ship shall be properly documented to evidence neutrality of the subject matter where there is a warranty of neutrality.
- (b) The adventure is lawful and is going to be carried in a lawful manner.

#### **Liability of the insurer :**

The general rule is that in case of loss due to the perils insured against, the insurer must indemnify the assured to the extent he has undertaken to do so under the policy. But in order to make the insurer liable it must be proved that the loss is the proximate result of one or the other perils insured against. The principle of the insurer's liability is that where there is a loss due to a combin-

<sup>1</sup> Provincial Insurance Co. of Canada *vs.* Leduc, (1874) L.R. 6 P.C.

<sup>2</sup> See the chapter on Carriers for a discussion as to the meaning of seaworthiness.

tion of causes operating at or about the same time, the proximate cause of the loss will be the cause which is the dominant or effective cause and this is not necessarily the cause which occurs last in point of time.<sup>1</sup> If the proximate cause is one of the perils insured against, the insurer is liable. Thus where a ship was settled by her crew it was held by the House of Lords that the proximate cause of the loss was not the entry of sea water into the ship, but the act of the crew and hence the insurer was not liable<sup>2</sup>.

The insurer is liable if the loss is caused by the perils insured against even if the loss might have been avoided but for the negligence or misconduct of the master or the crew, unless such negligence or misconduct is wilful<sup>3</sup>. The insurer is not liable for loss which is incidental to property such as loss by decomposition, as of meat, fruit, flour, or is caused by worms, rats or vermin or the ordinary leakage or breakage and so on.

#### **Insurable Interest :**

In a marine policy every person has an insurable interest who is interested in a marine adventure. In particular a person is interested in a marine adventure where he stands in any legal or equitable relation to the adventure or to any insurable property or risk therein, in consequence of which he may benefit by the safety or due arrival of insurable property, or may be prejudiced by its loss, or by damage thereto or by the detention thereof, or may incur liability in respect thereof<sup>4</sup>. Ownership or a vested interest in possession is not necessary to constitute an insurable interest. Thus the ship or the cargo may be insured by a lender of money by way of mortgage, bottomry or respondentia or the freight payable on arrival of goods or under charterparty may be insured by the shipowner. The ship or cargo may be insured by a captain or any other person who has a lien on them for wages or by a purchaser who has contracted to buy the cargo on arrival.

#### **Assignment of Marine Policy :**

A marine policy is not an incident to the property insured. Where, therefore, the assured assigns or otherwise parts with the

<sup>1</sup> Samuel *vs.* Dumas (1924) A.C. 431.

<sup>2</sup> *Ibid.*

<sup>3</sup> Marine Insurance Act, 1906, S. 5 (1) & (2).

<sup>4</sup> Marine Insurance Act, 1906, S. 55 (2).

subject matter insured, he does not thereby transfer to the assignee his rights under the contract of insurance, unless there be an express or implied agreement with the assignee to the effect.<sup>1</sup> But this does not affect transmission of interest by the operation of law, e.g., where in case of death of the assured, his heirs become entitled to the benefit of the policy or in the case of bankruptcy of the assured, the Receiver or the official assignee in bankruptcy becomes entitled to the benefit of the policy.

A marine policy is assignable either before or after loss unless it contains terms expressly prohibiting assignment and it may be assigned by endorsement thereon or in any other customary manner. In India the only statutory requirement for assignment is S. 130A of the Transfer of Property (Amendment) Act 1944. Before loss a policy can be assigned only to a person who has acquired some interest in the property e.g. to a purchaser or a mortgagee, otherwise the assignee will have no insurable interest in the insured property at the time of the loss and will not be entitled to sue on the policy. But once the assured has parted with or lost his interest in the subject matter insured and has not before or at the time of so doing expressly or impliedly agreed to assign the policy, any subsequent assignment of the policy before loss is bad and the policy will be of no effect. If however he has agreed to assign the policy to the transferee before or at the time of the transfer, the transferee can always maintain an action on the policy in the name of the assured.<sup>2</sup> But after loss an assignment may be made to any person whether he has any interest in the insured property or not and the assignee acquires all the rights which the assignor had on the policy.<sup>3</sup>

On a valid assignment the assignee becomes entitled to all the benefits under the contract and can sue the insurer on the contract in his own name.

<sup>1</sup> The Marine Insurance Act 1906, S. 51 Transfer of Property (Amendment) Act, 1944, S. 130A.

<sup>2</sup> Ibid, S. 50 (1) & (3), Transfer of Property (Amendment) Act 1944 S. 130A.

<sup>3</sup> Marine Insurance Act 1906 S. 51 Transfer of Property (Amendment) Act, 1944, S. 130A.

<sup>4</sup> Powles v. Jones (1844), 11 M. & W. 10.

<sup>5</sup> Aron & Co. v. Mill, (1923) 34 Com. Cas. 18, Transfer of Property (Amendment) Act, 1944, S. 130A.

### Avoidance of Contract :

A contract of marine insurance is voidable at the option of the under-writer on the ground of fraud, misrepresentation and non-disclosure of material facts by assured. As a contract of marine insurance is a contract *uberrimae fidei* the assured must disclose to the insurer before the contract is concluded every material circumstance which is known to the assured, and the assured is deemed to know any circumstance which, in the ordinary course of business ought to be known by him. If the assured

fails to make such disclosure the insurer may avoid the contract.<sup>1</sup> Every circumstance is material which would influence the judgement of a prudent insurer in fixing the premium or determining whether he will take the risk. But the following circumstances need not be disclosed:—(a) any circumstance which diminishes the risk, (b) any circumstance which is known by the insurer or which he is presumed to know, e., matters of common knowledge or notoriety, (c) any circumstance as to which information is waived by the insuree, (d) any circumstance which it is superfluous to disclose by reason of any express implied warranty.

The law relating to misrepresentation in marine insurance is contained in the Marine Insurance Act which is as follows:

- (a) Every material representation made by the assured or his agent to the insurer during the negotiation for the contract and before the contract is concluded must be true. If it is untrue the insurer may avoid a contract.
- (b) A representation is material which would influence the judgement of a prudent insurer in fixing the premium or determining whether he will take the risk.
- (c) A representation may be either a representation as to a matter of fact or a statement of expectation or belief.
- (d) A representation is considered material if it be substantially untrue—that is to say if the difference between what is represented and what is actually correct would not be considered material by a prudent insurer.

<sup>1</sup> Marine Insurance Act 1906 § 16 (1)

<sup>2</sup> Ibid. S 16 (2)

<sup>3</sup> Ibid. S 18 (3)

<sup>4</sup> S 20.

- (e) A representation as to a matter of expectation or belief is true if it be made in good faith
- (f) A representation may be withdrawn or rejected before the contract is concluded.
- (g) Whether a particular representation be material or not is, in each case, a question of fact

A representation may be in writing or verbal and may be innocent or fraudulent. Whether a representation is innocent or fraudulent the legal effect is the same. If the representation turns out to be untrue the policy will be avoided provided the representation is material.

### **Result of the Contract :**

If the property insured reaches its destination in safety in the case of a voyage policy or, in the case of a time policy remains safe until after the expiry of the stipulated time, the under writer is no longer liable on the policy. But in case of loss by any of the perils insured against the under writer must indemnify for the loss. Now loss may be either total or partial. Total loss is either 'actual total loss' or constructive total loss. Partial loss may be either due to particular average or general average loss. We shall discuss below these different kinds of loss.

### **Total Loss :**

A total loss is of two kinds viz (1) actual or absolute & (2) constructive.

(1) Where the subject matter insured is destroyed or damaged so as to cease to be a thing of the kind insured or where the assured is irretrievably deprived thereof there is an actual total loss.<sup>1</sup> This definition covers two cases - (a) where the subject matter undergoes such a change as to cease to be the thing originally insured. Thus, if a ship is wrecked and dismantled so as to completely lose her character as a ship, there is an actual total loss. (b) where the assured loses the possession of the subject matter for good. Thus if the ship

<sup>1</sup> Marine Insurance Act, 1906, S 57 (1)

<sup>2</sup> Cambridge vs Anderton, (1824) 2 B. & C. 691, Irving vs Manning, (1847), 1 H.L. 287

founders in mid-ocean, and there is no chance of raising her or the goods on board her, there is also an actual total loss.

But it should be noted that where goods reach their destination in specie, but by reason of obliteration of marks, or otherwise, they are incapable of identification, the loss, if any, is partial, not total<sup>1</sup>. The reason is that the goods have not perished or become different but have only become incapable of being sorted out by their owners, e.g., where 50 bags of flour belonging to A have become mixed up with 50 bags of flour belonging to B. In such a case the owners become tenants in common<sup>2</sup> i.e., joint owners having their shares ascertained. If there is any loss in the sale price, the loss is only partial.

(2) Subject to any express provisions in the policy, there is a constructive total loss where the subject matter insured is reasonably abandoned on account of its actual total loss appearing to be unavoidable, or because it could not be preserved from actual total loss without an expenditure which would exceed its value when the expenditure has been incurred<sup>3</sup>.

In particular there is a constructive total loss<sup>4</sup>:—

- (i) Where the assured is deprived of the possession of his ship or goods by a peril insured against, and (a) it is unlikely that he can recover the ship or goods as the case may be, or (b) the cost of recovering the ship or goods, as the case may be, would exceed their value when recovered; or
- (ii) In the case of damage to a ship, where she is so damaged by a peril insured against that the cost of repairing the damage would exceed the value of the ship when repaired. In estimating the cost of repairing, no deduction is to be made in respect of general average contributions to those repairs payable by other interests, but account is to be taken of the expense of future salvage operations and of any future general average contributions to which the ship would be liable if repaired; or

<sup>1</sup> Marine Insurance Act, S. 56 (5).

<sup>2</sup> Spence *vs.* Union Marine Insurance Co., (1868), L.R. 3 C.P. 427.

<sup>3</sup> Marine Insurance Act, 1906, S. 60 (1).

<sup>4</sup> *Ibid.*, S. 60 (2).

(ii) In the case of damage to goods, where the cost of repairing the damage and forwarding the goods to their destination would exceed their value on arrival.

Where there is a constructive total loss the assured may either treat the loss as a partial loss, or abandon the subject matter insured to the insurer and treat the loss as if it were an actual total loss<sup>1</sup>.

A constructive total loss thus arises in two ways —

(a) Firstly the assured may, by the perils insured against be deprived of the possession of the insured property in circumstances which, make it unlikely that he can recover it within any assignable time e.g. when the insured property is captured by the enemy or by the assured's own government, or by pirates or the ship is deserted by the master and crew.

(b) Secondly, although the assured may not be so visibly dispossessed of the insured property it may be so damaged by the perils insured against that the cost of repairing the damage or of carrying the goods to the port of destination may be so great as would exceed their value<sup>2</sup>.

#### **Notice of abandonment :**

In the case of a constructive total loss the assured must elect as to whether he would claim partial loss or total loss. If he wants to claim total loss he must abandon all claims on the insured property and give notice of abandonment to the insurer. The law relating to notice of abandonment is contained in the Marine Insurance Act, 1906<sup>3</sup> which is as follows —

(1) Where the assured elects to abandon the subject matter insured to the insurer, he must give notice of abandonment. If he fails to do so the loss can be only treated as a partial loss.

(2) Notice of abandonment may be given in writing or by word of mouth; or partly in writing and partly by

<sup>1</sup> Marine Insurance Act, 1906, S 61

<sup>2</sup> *Ruys vs Royal Exchange Assurance Corporation*, (1897) 2 C.B. 13; *Roud vs Salvador*, (1836) 1 Bing NC 526, 3 Bing NC 266

<sup>3</sup> *Moss vs Smith*, (1850) 9 C.B. 94 103

<sup>4</sup> Ss 62 & 63.

word of mouth, and may be given in any terms which indicate the intention of the assured to abandon his insured interest in the subject matter insured unconditionally to the insurer.

- (3) Notice of abandonment must be given with reasonable diligence after the receipt of reliable information of the loss, but where the information is of a doubtful character the assured is entitled to a reasonable time to make enquiry.
- (4) Where notice of abandonment is properly given, the rights of the assured are not prejudiced by the fact that the insurer refuses to accept abandonment.
- (5) The acceptance of an abandonment may be either express or implied from the conduct of the insurer. The mere silence of the insurer after notice is not acceptance.
- (6) Where notice of abandonment is accepted the abandonment is irrevocable. The acceptance of the notice conclusively admits liability for the loss and the sufficiency of the notice. Thus the old law that the assured cannot recover total loss if the insured property were restored to him before he brought his action is no longer good.
- (7) Notice of abandonment is unnecessary where, at the time when the assured receives information of the loss, there would be no possibility of benefit to the insurer if notice were given to him.
- (8) Notice of abandonment may be waived by the insurer.
- (9) Where the insurer has insured his risk, no notice of abandonment need be given by him to the re-insurer.

Where there is a valid abandonment the insurer is entitled to take over the interest of the assured in whatever may remain of the subject matter insured and all proprietary rights incidental thereto.

Upon the abandonment of a ship, the insurer thereof is entitled to any freight in course of being earned, and which is earned by her subsequent to the casualty causing the loss, less the expenses of earning it incurred after the casualty; and, where the ship is carrying the owner's goods, the insurer is entitled to a reasonable remuneration for the carriage of them subsequent to the casualty causing the loss.

### **Partial Loss :**

Partial loss arises in two ways *viz.*, (a) where the subject matter insured is partly lost or damaged by a peril insured against e.g., when part of the goods insured is lost or the ship insured is damaged as when the mast is broken or the sail is ripped, (b) where the assured has to contribute rateably towards general loss concerning the whole adventure. The former is known as "particular average loss" and the latter is known as "general average loss."

### **Particular Average Loss :**

A particular average loss is any partial loss of the subject matter insured, which is not a general average loss<sup>1</sup>. It is a loss which concerns the subject matter insured alone and is caused by a peril insured against. Thus A sends a cargo of wheat along with other cargoes belonging to others. Part of the wheat is burnt by fire and no loss or expenditure is incurred to save the whole ship or the other cargoes. The loss is particular average. A insures his ship with B. The mast is broken by high winds. No loss or expense is incurred to save the whole ship or the cargo on board. The loss is particular average. A, the owner of a ship carrying goods, insures the freight which is payable on safe arrival. Part of the cargo is washed away by water. The loss of freight on the lost cargo is particular average.

### **Measure of Particular Average Loss :**

The calculation of particular average loss is done differently for different subject matters as will appear below :

(a) *Particular average on ship* :—If a ship which is insured is damaged, the owner is entitled, subject to express terms in the policy, to the reasonable costs of repairs, less the customary deductions, where he has repaired the damage. If, however, the ship has not been repaired or has been only partially repaired, the assured can recover reasonable costs of such repairs (if any) as have been done and indemnity for the reasonable depreciation arising from the unrepaired damage not exceeding the reasonable cost of repairing the same. In any case the assured cannot recover more than the insured sum.

<sup>1</sup> Marine Insurance Act, 1906, S. 64 (1).

(b) *Particular average on goods* — In case of damage to goods insured, the particular average loss is calculated in the following manner. The difference between the gross value of the goods on their arrival at the port of destination and what would have been their gross value had they not been damaged is first ascertained. The difference gives the loss or depreciation on the gross value of the goods had they arrived undamaged. From that we arrive at the proportionate loss on the original value of the goods, which loss the insurer must pay. Thus suppose the original value of the goods was Rs 100/. The goods would have sold for Rs 200 at the port of destination were they not damaged, but sell for Rs 150 in their damaged state. Then the loss or depreciation on Rs 200 is Rs 50/ (Rs 200 - Rs 150). Therefore the loss or depreciation on Rs 100 (the original value) is Rs 25. The cts. Rs 25 is the particular average loss which the Insurer will pay. The reason for this in that in calculation is that the assured ought not to allow a to make a profit by insurance and he cannot recover anything more than he originally paid.

(c) *Particular average on freight* — When a part of the freight is lost by a loss of a part of the cargo the insurer pays the same proportion of the value insured as the freight lost bears to the total of full cargo. Thus if the freight of a full cargo insured for Rs 10,000 and 10% of the cargo is lost the insurer will pay 10% of Rs 10,000 i.e. Rs 1000.

### **General Average Loss :**

A general average loss is a loss caused by or directly consequential on a general average act.<sup>1</sup> A general average act means any act which is reasonably undertaken for the common safety of all interests connected in a maritime adventure e.g. those of cargo owners, shipowners, charterers and so on. It includes (a) general average expenditure e.g. remuneration paid to salvors at the time of peril to save the whole of the property at risk<sup>2</sup>, or the money paid to pirates for the purpose of saving

<sup>1</sup> Marine Insurance Act, 1906, S 66 (1)

<sup>2</sup> Ocean steamship *ss Anderson* (1883) 13a B.D. 631 C.A. 19

both ship and cargo<sup>1</sup> or inward expenses including towage, pilotage, harbour dues etc., paid while the ship takes refuge into a port for her own safety and that of the cargo on board her, and also

(b) general average sacrifice e.g., where holes are cut in the ship and goods are thrown into the sea for the sake of lightening her or water is thrown down a ship's hatches to extinguish an accidental fire and other goods are damaged thereby

**Contribution** Where there is general average expenditure or sacrifice there is a general average loss. If there is a general average loss, the party on whom the loss falls is entitled, unless the peril causing the loss has been occasioned by his own or his servant's fault, to a ratable contribution from the other parties interested in the adventure and for whose common safety the loss has been occasioned. Such contribution is known as general average contribution. Thus if a hole is cut in the ship to remove weight to lighten her or the mast is broken off to save her in such a case the shipowner is entitled to contribution from the charterer and other persons interested in the ship, ratably to the general average loss suffered by the shipowner. But since the sacrifice is made in safety of the owner, the charterer and other persons interested in the ship are liable ratably to the general average loss suffered by the shipowner while extinguishing a fire the owner of the goods suffers only the loss. But he is entitled to ratable contribution from the other parties interested in the adventure.

There is fundamental difference between general average loss and a particular average loss. The former is the result of a general average act undertaken for common safety and is therefore, made good by contribution from all parties concerned in the adventure. The latter is however due to a maritime peril affecting only the interest of the party on whom the loss originally fell.

We have seen that in the case of general average loss all parties interested in the adventure are liable to contribute ratably. Therefore for each party the amount of his contribution is deemed to be partial loss which he is entitled to recover from his respective insurer.

<sup>1</sup> *Whitcrown Wire vs Savill*, (1882), 5 QBD 651, C.A.

Where the assured has incurred 'general Average expenditure' it cannot recover the whole of such expenditure from his insurer. The insurer is liable to indemnify him only to the extent of his contribution. Thus shipowner paying money to pirates to save the ship and cargo cannot recover the whole amount from his insurer. He would be entitled to get only that amount which will be adjusted in his account after due regard to account the contribution which the cargo owner and other interested parties are liable to make. If he fails to do so or he resolute to such other persons for a greater sum, he will sacrifice the assured to receive from the insurer the full amount of the loss, the remainder being treated as a debt of the assured in respect of his right against the other persons. Thus in the case of a gun boat blown up by a hole being cut in the hull, if the assured had resolute to claim the shipowner in the first instance, he would not be able to recover the loss from the insurer subject to his liability under the policy, when the assured had paid a sum less than the amount of his loss to the shipowner. Thus if goods are thrown overboard in the ship the ship owner who has to pay a general contribution can recover the amount from his insurer.

### The Rights of the Insurer :

The following are the rights of the insurer in a marine policy :-  
 (1) He is entitled to payment of the premium stipulated in the policy.

(2) He is entitled to avoid the contract if there is any fraud, misrepresentation or nondisclosure of material facts or any unauthorised alteration of any material term of the policy without his consent, or any breach of warranty.

(3) He is entitled to the right of the assured and he is entitled to all the rights and remedies of the assured, on his indemnifying the assured, in the following cases :—

(1) Where there is a total loss, either actual or constructive, the assured having abandoned the property insured, the insurer is entitled to all the materials salvaged or to the property if and when restored. He

<sup>1</sup> Marine Insurance Act, (1906), S. 66 (4).

is also entitled to all claims in damages which the assured may have against third parties in respect of negligence or tort due to which the total loss is caused. Thus if a ship insured is totally lost as a result of collision with another ship caused by the negligence of the owner of the other ship or his servants, the owner of the insured ship has a claim for damages against the latter shipowner. If he is indemnified by his insurer, the insurer is entitled to the damages which he may recover against the latter shipowner.

- (2) Where a general average loss occurs as a result of general average sacrifice the insurer of the party on whom the loss falls indemnifies for the entire loss. But the insurer is subrogated to the rights of the assured and he is entitled to general average contribution which the other parties interested in the adventure are liable to make.

### **Fire Insurance :**

In India there is no statute like the English Gambling Act of 1774 dealing with contract of fire insurance. The law on the subject to be applied to India is, therefore, English law and the principles established by Indian decisions subject always to the provisions of the Indian Contract Act and Indian Stamp Act.

### **Nature and form of the Contract :**

A contract of fire insurance has been defined in Halsbury's Laws of England<sup>1</sup> as a contract by which the insurer agrees, for a valuable consideration (usually called the premium) to indemnify the assured, upto a certain amount and subject to certain terms and conditions, against loss or injury by fire which may happen to the property insured during a specified period. The contract is usually embodied in a policy which contains all the terms and conditions on which the insurance is effected. But the contract may be concluded by the acceptance of the proposal by the insurer before any premium is paid or policy issued. When such a contract is concluded the insurer may be compelled to issue a policy even if a fire has already taken place.<sup>2</sup>

<sup>1</sup> Vol. XVII, p. 516.

<sup>2</sup> Bhugwandas *vs.* Netherlands India Sea and Fire Insurance Co. of Batavia, (1888), 14 A.C. 83 P.C.

### **Formation of Contract :**

A contract of fire insurance is usually concluded in the following manner. The insured, to begin with fills up his proposal in a printed form supplied by an agent of the insurer. On fulfilling the proposal the insured sends the premium or some part of it to the insurer who thereupon issues what is known as a deposit receipt or interim protection note often called a cover note whereby he undertakes to keep the insured indemnified for a limited period until the acceptance or rejection of the proposal of the insured. The cover note is evidence of the proposal and also certifies in writing that pending the acceptance or rejection of the proposal the party or the insured would remain insured subject to the terms and conditions of the insurance. If any fire takes place during the currency of the cover note the insurer will cover the loss unless he has previously declined the proposal. When the insurer accepts the proposal a regular policy is issued. The insured at once will be informed of conditions subject to which the policy will be.

### **Insurable Interest :**

We have already noticed what insurable interest signifies. The insured in the policy must have some interest in the subject matter not only at the time of loss but also at the time of effecting the policy according to English law. But the English Life Assurance Act, 1774 does not apply to India and it seems likely that in India it is enough if the insured has some interest at the time of loss. This is also in accord with the principles of marine insurance. It has been held that the following persons have an insurable interest in the following properties so as to enable them to effect fire insurance thereon:

- (a) A vendor of goods in respect of which the property and risk have not passed
- (b) The mortgagor and mortgagee of any property, moveable or immoveable
- (c) The trustee and beneficiary of any property
- (d) The lessor and lessee of any property
- (e) The bailor or bailee of any property

<sup>1</sup> Life Assurance Act, 1774, Sec 1, 2 & 4.

### **Contract 'uberrimae Fidei' :**

A contract of fire insurance is like all insurance contracts a contract *uberrimae fidei* and the assured must disclose all material facts, *i.e.*, facts which determine the question of premium and risk, within his knowledge. If he fails to do so the insurer may avoid the contract. The following have been held to be material facts which must be disclosed by the assured even when no question relating to them are asked (though in fact they are usually asked).

- (a) whether there are other insurances on the same property,
- (b) whether other insurers have refused insurance on the same property.
- (c) whether there occurred previous fires on the same premises or in the neighbourhood,
- (d) of what materials, the outer walls, roof, etc., of the house are made of,
- (e) for what purpose the building or premises are used,
- (f) whether the building is occupied or not.

The rules relating to non-disclosure of material facts applicable to marine Insurance including those relating to facts which need not be disclosed are equally applicable to fire insurance subject, however, to the express terms of the policy .

### **Representations and Warranties :**

In the written proposal which the assured signs are contained statements and answers to questions *e.g.*, the description of the property, or the nature of neighbouring risks, or whether the assured has had a fire claim against any office. Such statements and answers are called representations and if any representation material to the risk is not substantially true the insurer is entitled to avoid the contract. If such statements and answers are embodied in the policy itself they amount to what are called warranties and it is a condition precedent of the insurer's liability that the warranties must be strictly and literally true whether they are material to the risk or not. Thus if the subject matter is warranted to be of a particular nature or description, it must be exactly that which it is warranted to be. Therefore if a mill is insured warranted as "conformable to the first class of mill rates," and in fact the mill is not conformable to such first class of mill rates, the policy will be held void, although it be clearly proved that the deviation from the warranty did not at all increase the

risk.<sup>1</sup> But it has been held that a reasonable construction should be given even to a warranty. Thus where there was a warranty that certain cotton mills were worked by day only, it was held that there was no breach of warranty if the engines and the unconnected shafting went all night, the mill and machinery not being substantially worked. So also where a policy was in premises warranted as "where no fire is kept, and where no hazardous goods are deposited" it was held that the word kept might habitually kept. A fire caused therefore, by making a fire and bringing a barrel on the premises to repair them would not deprive the assured from claiming the loss.

#### Different kinds of Fire Policy :

A fire insurance policy like that of marine insurance may be either valued or unvalued.<sup>2</sup> But an unvalued policy is not common in fire insurance. A valued policy is one which specifies the agreed value of the subject matter and which in the absence of fraud, is conclusive as against the insurer who must pay the agreed amount in case of total loss. An unvalued or open policy is one which does not specify the value of the subject matter but subject to the limit of the sum insured leaves the value of subject matter to be determined subsequently. In case of fire insurance unlike marine insurance, the value of the subject matter in an unvalued policy is ascertained as at the date of re-insurance and not at the date of the conclusion of the contract.

A blanket and floating policy is one which does not attach to any specific or ascertained property. It is generally issued to factors or to persons interested only to cover margins unmet by other policies or to cover the limited liability which they may have in the property in their charge. It is clear that the quantity of property covered by a floating policy is subject to daily fluctuations due to sales, removals, replacements or additions.

A specific policy is one in which the property is insured for a

<sup>1</sup> New Castle Fire Insurance Co. vs. Macmorran & Co., (1815) 3 Dow, 255 H.L.

<sup>2</sup> Mayall vs. Milford, (1837) 6 Ad & El 670, Whitehead vs. Price (1835) 2 G.M. & R. 447

<sup>3</sup> Drbean vs. Sotheby, (1827) Mood & M. 90

**specific sum** and is not subject to average. In case of loss the insurer is liable to pay the full amount of the loss, **Specific and Average policies** up to the limit of the insured sum. An **average policy** is one which stipulates that in case the property is undervalued a portion of the loss will be borne by the assured and the insurer will be liable for such proportion only of the loss as the amount insured bears to the value of the property. An average policy is constituted by inserting the 'average clause' in the policy. Floating policies generally contain the average clause.

### Conditions Precedent in a Fire Policy :

A fire policy generally contains certain conditions the fulfillment of which is a condition precedent for enabling the assured to recover loss or damage caused by fire. Bunyon in his book on fire Insurance<sup>1</sup> has referred to the usual conditions which are as follows : -

- (i) Notice must be given by the assured to the insurer of anything done in respect of the property insured whereby the risk is increased.
- (ii) The assured must give the particulars of the property and risk covered.
- (iii) The assured must give notice of loss without unreasonable delay and deliver his claim giving all the necessary particulars with sufficient proofs thereof within a prescribed time.
- (iv) Any fraudulent claim is when it is wilfully filed in any substantial respect, by the assured would cause forfeiture of all benefits under the policy.
- (v) In case of difference in respect of the amount of loss or damage such difference is to be referred to arbitration as a condition precedent to any action by the assured, within prescribed period.

### Assignment of Policy :

"A contract of fire insurance is a personal contract with the assured, and is not a contract passing with the property insured."<sup>2</sup>

<sup>1</sup> Bunyon on Fire Insurance, 5th ed., p. 96.

<sup>2</sup> Halsbury's Laws of England, Vol. xvii, p. 517.

Therefore, on a sale or transfer of the property, the transferee acquires no interest in the policy, unless the policy is expressly or impliedly assigned to him. Thus if a vendor who has insured property against fire conveys it to purchaser without assigning the policy and the property is burnt down, the policy will not be available to either the vendor or the purchaser. The vendor can not recover because he has ceased to have any interest at the date of loss<sup>1</sup> and the purchaser also cannot recover because the policy was not assigned to him. So strict is this rule that it has been held that where the vendor who has insured his house against fire contracts to sell it and between the date of the contract and its completion the house is damaged by fire, and the insurance company, not being aware of the accident, pays the amount of the loss to the vendor, the purchaser cannot sue against the vendor to recover the insurance money as an element of the purchase money. In such a case the insurance company can compel the vendor to refund the money they have paid if the vendor receives the whole of the purchase money the reason being that the insurance being a contract of indemnity the assured cannot recover any loss which he suffered in less.

In the absence of any express provision prohibiting assignment a fire insurance policy may be assigned by writing either by indorsement on the policy or in any other customary manner. But the assured must have some insurable interest at the time of assignment and if he puts up or loses his interest in the property insured in assignment therewith by him will be of no effect. Before loss the policy can only be assigned to a person who has acquired some interest in the property e.g. the purchaser, or a mortgagor or bailee or pledgee but otherwise the assignee will have no insurable interest in the subject matter at the date of loss. After loss however the policy may be assigned to any person whether he has any interest in the subject matter or not.

Porter seems to take the view that a fire insurance policy, being a personal contract is not assignable without the consent of the insurer.<sup>4</sup> This view seems to have been based on the deci-

<sup>1</sup> *Poole vs Adams* (1864) 33 L.J.Ch. 639

<sup>2</sup> *Raynor vs Preston* (1883) 18 Ch.D.I.C.A.

<sup>3</sup> *Castellion vs Preston* (1883) 11 Q.B.D. 380 C.A.

<sup>4</sup> *Porter on Insurance* 6th ed., p. 301

sions in *Lynch vs. Dalzell*<sup>1</sup> and *Sadlers Co. vs. Badcock*.<sup>2</sup> But there does not seem to be any reason why a fire insurance policy should alone be subject to this restriction. A marine insurance policy or a sale of goods is as much a personal contract as fire insurance and if the benefits under the first class of contracts can be assigned without the consent of the party liable thereunder it seems illogical to hold that assignment of a fire policy alone should be subject to the consent of the insurer. In fact this view has gained ground because a Fire insurance policy generally contains the following clause—

“This policy ceases to be in force as to any of the property hereby insured, which shall pass from the insured to any other person otherwise than by will or operation of law, unless notice thereof be given to the company and the subsistence of the insurance in favour of such other person be declared by a memorandum indorsed thereon by or on behalf of the company.”

In the absence of such a clause there seems to be no reason to hold that an assignment to be valid must be with the consent of the insurer. In India the law seems to be more clear. Under S. 135 of the Transfer of Property Act all that is required for a valid assignment is that it must be by an endorsement or any other writing. Notice to the insurer of the assignment is necessary only to make him liable to the assignee if he pays the money due to the assured even after such notice.

On a valid assignment the assignee becomes entitled to all the benefit under the contract and can sue the insurer on the contract in his own name.

#### Liability of the Insurer :

In a fire policy the assured is entitled to recover any loss or damage by fire to the property insured. A loss by fire means loss by ignition and does not include loss or damage by heating where nothing has caught fire. Thus where due to the negligence of the servants of the assured smoke and heat from a store are forced into a room and do damage to goods, the insurer is not liable to make good the damage.<sup>3</sup> All that the assured has

<sup>1</sup> (1730), 4 Br. Parl. Cas. 431.

<sup>2</sup> (1743), 2 Atk., 554.

<sup>3</sup> *Austin vs. Drew* (1815) 4 Camp. 360; (1815), 6 Taut. 436.

to prove is that the loss has been caused by fire. The cause is immaterial and it is no defence for the insurer that the fire would not have been caused but for the negligence of the insured or his servants<sup>1</sup>. But the assured must prove that fire or some peril insured against in the policy was the proximate cause of the loss. Proximate cause means the dominant or effective or direct cause and not necessarily the last cause in a chain or combination of causes.

Thus it has been held that where damage is caused to the insured property as a result of explosion of gunpowder, at a distance of half a mile from the premises, the loss and damage is not to be regarded as caused by fire. Remote damages which result from, but are not the direct consequence of a fire, e.g. loss of profits or rent due to goods or houses being burnt are not recoverable unless specially insured. But certain losses are so necessarily connected with fire that they are recoverable even though not directly caused. Thus a loss due to bonfire efforts to put out a fire is recoverable from further loss of damage by water or by the wind or of furniture or by theft of goods in the course of removal are recoverable. The insured cannot however recover any loss caused by his own wilful misconduct, whether it actually relates to the property insured on the principle that he is liable for all loss proximately caused by himself. Insured in respect of his conduct if the same is caused by another party.

As we have already seen the insurance policy generally contains a clause which provides that the assured must be fully indemnified for his insured property against all risks to the property. Thus the assured must give notice of the loss without unreasonable delay and limit his claim to sufficient payment. This is within the prescribed time and less from the loss or whatever sum paid may be precluded.

<sup>1</sup> Jameson *vs* Royal Insurance Co. 71 R.C.J. 126

- Becker Gray & Co. *vs* London Assurance Corporation (1918) 4 C.H.R. 112

<sup>2</sup> Everett *vs* London Assurance Co. (1865), 19 C.B. (N.S.) 126

<sup>3</sup> Observation of Kelly C. B. in Stanley *vs* Western Ins. Co. (1964)

<sup>4</sup> R. 3 Ex Ch. 71

Busk *vs* Royal Exchange Assurance Co., (1818) 2 B. & Ald. 77

If there is any arbitration clause in the condition, as there was, to the effect that in case of any difference as to the amount of loss or damage, the same should be referred to arbitration, the assured must go to arbitration and obtain in award his agreed amount of damages before he can found an action against the insurer.<sup>1</sup> But it has been held by the House of Lords in *Juridini v. National Path Insurance Co.*<sup>2</sup> that where the insurer repudiates his liability in toto on the ground of fraud, usury or otherwise that the repudiation goes to the substance of the whole contract the assured need not go to arbitration and can institute a suit at once for the recovery of the damage or loss. In the recent decision of the House of Lords in *Heyman v. D'Avins* the principle laid down in *Juridini's* case has however been doubted and it seems that the safest course for the assured, in the case of a difference as to the amount of damages and repudiation of liability by the insured, is to go to arbitration and have in award to damages before he institutes a suit to recover of the amount awarded as damages by arbitration. In the recent unreported case of *Binechind Marikhur v. Concord of India Insurance Ltd.* the facts were very similar to *Juridini's* case. The Insurance Co. repudiated the whole claim of the plaintiff on the ground of usury and fraudulent claim. But before such repudiation the parties had come to an agreement as to amount of damages. The case was heard in the first instance by Pinckridge J. before the decision in *Heyman v. D'Avins* was reported. It was held by him following *Juridini's* case that as there was a total repudiation of the plaintiff's claim, it was not necessary for him to go to arbitration. On appeal it was held by Gentle J. and Sen J. that even if *Heyman's* case be regarded as modifying the law laid down in *Juridini's* case, there was no need to go to arbitration as the amount of damage was agreed upon between the parties and there was no difference as to the sum and the fact that the plaintiff did not go to arbitration would not bar the plaintiff's claim as to the agreed amount. It was case of denial of my liability whatever and not a case of merely disputing the liability to pay the amount claimed by the plaintiff.

<sup>1</sup> *Scott vs Avery* (1856), 5 H.L. Cas. 811

<sup>2</sup> (1915) A.C. 499

<sup>3</sup> (1941) A.C.

**Amount Recoverable :**

In marine insurance, as we have already seen, the insurer is liable to pay the whole of the amount insured in case of total loss and a proportion only of the loss as the insured amount bears to the value of the property in case of partial loss. But in fire insurance the insurer is liable to pay for the actual loss upto the amount insured whether the loss be total or partial in the absence of any express provision to the contrary. Thus if the value of the property insured be Rs. 10,000/- and the amount insured is Rs. 1000/- and partial loss occurs to the extent of 10 per cent, the fire insurance company will be liable to pay the entire amount of the loss namely Rs. 1000/- whereas if it were a marine insurance, the insurer would be liable to pay only 10 per cent of Rs. 1000/- i.e., Rs. 100/-

**Average :**

A fire insurance Company may however, limit its liability to pay the whole of the amount of the loss where it is partial by inserting what is known as "the average clause" in the policy. The effect of the average clause is that if at the date of loss the property insured is of greater value than the sum insured, then the assured shall be considered his own insurer for the difference and shall bear a rateable share of the loss accordingly and the insurer shall be liable for a proportion only of the loss as the insured amount bears to the value of the property<sup>1</sup>. Thus if in the above illustration the fire policy were subject to average, the fire insurance Company would have been liable to the extent of Rs. 100/- only and not Rs. 1000/-. The effect of the average clause is to bring fire insurance in line with marine insurance.

**Rights and Duties of Insurers :**

The insurer under a fire insurance policy has the following rights and duties :—

(1) *Entry on the premises and salvage* :—By custom and usage and in modern times by virtue of a specific clause generally inserted in a fire insurance policy, the insurers have the right in the event of loss or damage to the insured property to enter upon the premises which are insured or in which the subject matter of insurance is situate for the purpose of ascertaining the damage and protecting

<sup>1</sup> *Acme Wood Flooring Co. Ltd. vs. Marten* (1984) 9 Com. Cas. 157

it from further damage or loss and to retain possession for a reasonable time. But if the insurers remain in possession for an unreasonable time and the assured suffers loss or damage thereby they become liable in damages to the assured.<sup>1</sup>

(2) *Restatement*—Fire policies always contain a clause giving the insurers the option to reinstate the property insured in case of damage or loss in incidence to the payment of the claim in respect of such loss or damage. When a loss occurs the insurers have to make an election i.e. whether they will reinstate the property or pay for the claim. But once the insurers elect to reinstate, their liability to reinstate becomes absolute as if the policy contained an express stipulation to reinstate the property if case of loss or damage by fire and the insurers cannot choose subsequent to paying the sum to the reinstatement even if reinstatement becomes difficult or impossible. Thus in *Brown vs Roy*<sup>2</sup> In 1890 C. L. J. there is follows. The defendant 'n' a Coal dealer received 1000 bags of coal after they were damaged by fire. Whilst they were proceeding to reinstate the premises became dangerous and were caused to be removed by the Commissioners of Sewer under the provisions of the Building Act. The Insurance Company contended that reinstatement had become impossible by such removal. It was held that this contention was bad and that the Insurance Company having made their election to reinstate were absolutely bound to do what they had elected to do. In order to protect themselves against such contingencies as in Brown's case insurance Companies frequently insert clauses in the policy exempting them from liability to reinstate under certain circumstances.

(3) *Subrogation*—When the insurer has paid the whole of the loss sustained by the assured, whether total or partial, he is entitled to be subrogated to all the rights of the assured i.e., to the advantage of every right of the assured, whether such right consists in contract or in remedy for tort, or to any other right by which the loss can be or has been diminished e.g. the receipt of any money or the right to recover such money from third parties.<sup>3</sup>

<sup>1</sup> *Oldfield vs Price* (1860), 2 F & F 80

<sup>2</sup> (1899) 1 E & E 853

<sup>3</sup> *Bunyan*, Law of Fire Insurance, 5th ed., p. 228

<sup>4</sup> *Castellion vs Preston* (1883) 11 Q.B.D. 380, C.A. or Brett L.J., at

Thus where the lessor of a house is bound by covenant under the lease to repair and the house is burnt down by fire, the lessor who has insured the house can recover the loss from the insurer. If the insured money is sufficient to cover the whole loss and the insurer pays the sum he is subrogated to the rights of the lessor. If the lessor repairs the loss the lessor is bound to return the money paid to the insurer. If the lessor does not repair, the insurer can sue him in the name of the lessor on the covenant. The insurer can similarly sue in the name of the lessor third parties for whose negligence the lessor had been compelled to suffer damages. In the same way if the insured arises damages from third parties who have caused the injury he must pay the amount to the insurer and if he forgoes any sum received in such third party he will have to give up his right to sue.

But it should be noted that it is only payment of the whole of the loss that the insurer is entitled to make so that if the amount insured is less than the amount of the loss the insurer would not be subrogated to the rights of the lessor even though he has paid the amount insured. In such case he insured alone is being sued by a third party who may be liable to pay for the loss. But even in such case the assured must make over all his rights up to the amount of the loss which he may recover from the third party with whom he has suffered the principal loss. This is known as contribution and that is he has a right when recovering the amount over and above his own liability to sue the third party.

(4) *Salvoe*—This is the right of subrogation incidental to the right of subrogation. If the insurer pays the whole amount insured they are by the principles of subrogation entitled to the salvaging, that is the value and all that remains of the property after fire.

(5) *Contribution*. This right arises when the same subject matter is insured under several fire policies. When there are several policies on the same property an insurer may by inserting a clause in his policy limit his liability in the event of loss to only a rateable proportion of the loss. In such a case the assured can

<sup>1</sup> Commercial Union Assurance Co. *vs* Lister (1874) 9 Ch.D. 483.

<sup>2</sup> West of England Fire Insurance Co. *vs* Isaacs (1846) 2 Q.B. 377.

<sup>3</sup> Raynor *vs* Preston (1881) 18 Ch. D. 124.

not recover from the insurer more than the rateable proportion of the loss to which he is liable. But in the absence of such an express clause the insurer may recover from any insurer the whole amount he has insured without taking into account the amount he has insured with other insurers and if that does not cover the whole loss he can claim the remainder of the loss from others. "In such a case insurers amongst themselves contribute equally, if each company, is an insurer for an equal amount, and, if they are insurers in different amount then each company contributes in proportion to the amount it has insured."<sup>1</sup> Thus if company A has insured property to the extent of Rs. 1000/- and B to the extent of Rs. 500/-, the proportionate liability of B would be 1/3 and of A 2/3 for the whole loss when it occurs. If loss to the extent of Rs. 1000/- occurs the assured can recover from A the whole of Rs. 1000/- in the absence of any provision to the contrary. Then B would have to pay A one third of Rs. 1000/- . Or, if the assured recovers from B Rs. 500/- first and then recovers from A the remainder of the loss, B will then be entitled to recover from A Rs. 500/- less one third of Rs. 1000/- i.e., the excess over his liability paid by him.

#### **Life Insurance :**

There is no statute in India governing life insurance. The Insurance Act, 1938 deals with only certain aspects of life insurance e.g., agency, assignment, incorporation and winding up of insurance companies. The English law is still applicable to life insurance subject of course to the Indian Contract Act, Indian Stamp Act and the Insurance Act, 1938.

#### **Definition :**

Life insurance has been defined as a contract by which the insurer agrees upon the death of the person whose life is insured (commonly called the life insured) to pay a given sum in consideration of the payment by or on behalf of the assured during the continuance of the life of certain sums called premiums.<sup>2</sup> The contract of life insurance differs from fire or marine insurance in that it is not a contract of indemnity; for a man's life cannot be valued in terms of £. S. d. Thus a man may insure his life for any

<sup>1</sup> Halsbury's Laws of England, Vol. XVII, p. 36.

<sup>2</sup> Ibid, Vol. XVII, p. 543.

amount and on his death his heirs or representatives may recover the amount in full from the insurers. In certain types of policies e.g., endowment policy the assured may recover the sum insured after a specified period even if that be before the death of the assured.

#### **Difference between Life Insurance and other forms of Insurance :**

Life insurance differs from the other forms of insurance in the following respects :-

- (a) Fire, Marine and Accident insurance are contracts of indemnity. The assured cannot recover the whole of the amount insured if the loss be less than that and in no case can he recover more than the loss suffered by him and if there be no loss he cannot recover anything. But in case of life insurance the assured or his representatives can recover the whole of the amount insured on the happening of a particular event or on the expiry of a particular time.
- (b) The risk insured in case of fire, marine or accident insurance may not happen at all. But in life insurance the risk insured namely death is an event which must occur sometime or other. Thus the assured under fire or marine insurance policy may not get any part of the insured amount. But the assured or his representatives under a life policy is entitled to recover the whole of the insured amount.
- (c) A marine or fire insurance policy is for a fixed period e.g., a time policy or for a fixed purpose e.g., a Voyage policy and hence the period during which the risk will subsist is fairly ascertained. But a life policy is generally for a long term and may run during the whole of the duration of the assured's life. Hence the duration of the risk in a life policy is unascertained.
- (d) In a marine or fire policy the assured is required to have an insurable interest in terms of the policy and such interest is capable of valuation in terms of money. But in a life policy the insurable interest is one required by law and such interest cannot be measured in terms of money. Thus the interest of the owner of a cargo insured under a marine policy can be measured in terms

of money, his interest being the value of the cargo insured. But the interest of a son in the life of his father or that of a wife in her husband's life or the interest of a person in his own life is not capable of valuation in terms of money.

#### **Insurable Interest :**

We have discussed this subject in the beginning of this chapter. It is enough to state here that a man can take out an insurance on the life of any other person who is so connected with him as to make the continuance of the life of such a person a matter of some real or pecuniary interest for him. Such an interest would constitute the insurable interest required by law in a contract of life insurance. Thus it has been held that a husband and a wife have an insurable interest in the life of each other<sup>1</sup> on the ground that each is presumed to have a pecuniary interest in the life of the other. But a parent has no insurable interest in the life of his child as his child; nor has a child has an insurable interest in the life of his parent or parent. A creditor has also an insurable interest in the life of his debtor to the extent of the debt on the principle that the death of the debtor is supposed to diminish the chance of the creditor obtaining payment<sup>2</sup>. On the same principle a surety has been held to have an insurable interest in the life of the principal debtor against whom he has claim for indemnity in case he is compelled to pay the debt of the principal debtor<sup>3</sup>. So also one of two joint debtors or joint promisors has an insurable interest in the life of the other to the extent of one half of the debt or liability to which he would be entitled to contribution by the other in case he has to pay the whole debt<sup>4</sup>.

#### **Contract how made :**

A contract of life insurance like any other contract is made by the offer of the assured and acceptance of the same by the insurer. The proposal or offer is generally contained in a printed

<sup>1</sup> Reed v. Royal Exchange Assurance Co. (1795) Peake, Add Ch 70 Griffiths v. Fleming, (1909) 1 K.B. 805, C.A.

<sup>2</sup> Howard v. Refuge Friendly Society, (1886) 54 L.T. 644

<sup>3</sup> Anderson v. Eddie, (1795), 2 Park on Marine Insurance 8th ed., p. 914.

<sup>4</sup> Lee v. Hinton (1854), 5 De G.M. & G. 823, C.A.

<sup>5</sup> Bramford v. Bounder (1877), 25 W.R. 690

form prepared by the insurance company and delivered to the assured by an agent of the company and filled up by the assured. The printed form contains many enquiries concerning the age, habits and other facts relating to the assured's life. The assured must answer the enquiries in filling up the proposal form with care and caution as the falsity of any material particular will amount to misrepresentation which would avoid the policy. The proposal form is usually communicated to the company by its agent. The company then arranges for the medical examination of the assured. The doctor who conducts the medical examination must generally be one who is on the approved list of the company. The doctor submits a medical report after examining the assured which is a confidential report. The report contains the doctor's own findings as well as answers by the assured to the usual questions put by the doctor. After the medical report is submitted the company either accepts or rejects the proposal. The acceptance is generally communicated to the assured by a letter requesting the assured to remit the first instalment of the premium due. The contract is concluded as soon as this acceptance takes place.

#### Policy :

The contract is embodied in a document called the policy containing all the terms and conditions of the contract. The policy usually contains the names of the parties, amount and the risk insured, commencement and duration of risk, the amount of premium to be paid and the manner in which it has to be paid e.g., whether annually, quarterly, or in one lump. The policy also usually contains a clause that a grace of a certain number of days, generally a month for premium payable annually or quarterly would be allowed for the payment of an instalment of premium and that the policy would lapse if the assured makes default in paying the premium within the period of grace. But the policy also usually contains a clause providing for the revival of the policy after it so lapses on payment of all arrears of the premium with interest.

#### Representation and Warranties :

The statements and declarations made by the assured in the proposal form and also before the doctor are known as representations. The policy is voidable by the insurer if any material re-

presentation is untrue. But if the representations are embodied in the policy, as usually they are done, by expressly stipulating in the policy or in the conditions indorsed thereon, that the declarations are true and are to be taken as the basis of the contract, the representations become what are known as warranties. If any warranties, whether material or otherwise, turn out to be untrue the contract is avoided.

#### **Misrepresentation and Concealment :**

The law relating to misrepresentation and concealment is the same in respect of life insurance as with other forms of the insurance excepting that by S. 45 of the Insurance Act, 1938, no policy of life insurance effected before the commencement of the Act shall after the expiry of two years from the date of commencement of the Act and no policy of life insurance effected after the commencement of the Act shall, after the expiry of two years from the date on which it was effected, be called in question by an insurer on the ground that a statement made in the proposal or of any report of medical officer or referee or in any other document leading to the issue of the policy, was inaccurate or false, unless the insurer shows that such statement was on a material matter and fraudulently made by the policy holder who knew at the time of making it that the statement was false.

#### **Different kinds of Policies :**

The following are the different kinds of life policies in vogue in India —

(a) *Whole term assurance on single lives or a whole life policy*—This kind of policy stipulates the payment of a fixed sum, with or without profits on the death of the assured whenever that may occur. Usually the premium is fixed at an annual sum payable during the whole time of the continuance of the policy. But the premium may also be fixed at a lump sum payable once only at the time of the conclusion of the contract or at a limited number of payments, each larger than the annual premium, or at an annual sum payable at modified rate for a limited period and thereafter at a correspondingly higher rate.

(b) *Endowment assurance or policy*—In this kind of policy the sum insured is payable to the assured, with or with-

out profits, after a certain period or at a certain age should the assured live up to that time or to the representatives of the assured at his death if that be earlier. The premium is usually made payable annually for a fixed term of years, namely, upto the prescribed time or age at which the insured amount becomes payable to the assured if he survives.

- (c) *Insurance on joint lives*—In this kind of policy two or more lives are insured jointly and the sum insured becomes payable on the death of either or any of them to the survivor.
- (d) *Longest life assurance or insurance on last survivor*—In this kind of policy two or more lives are insured jointly but the sum insured becomes payable only on the death of the last survivor and not on the death of any one of the assured.

Insurance policies of this kind are mainly of two types which are as follows :—

1. *Temporary or short period insurance*—This kind of policy is effected on joint lives for short periods, the sum insured being payable, on the death of the last survivor only, if that occurs before the time specified.

2. *Survivorship Insurance, or on one life against another*—This kind of policy is effected on two lives jointly e.g., those of A and B so that the sum insured becomes payable on the death of A if that should occur before the death of B, but not otherwise. If B dies before A the amount insured cannot be recovered.

#### **Assignment :**

According to S. 38(1) of the Insurance Act, 1938, the assignment of a life policy can only be made by an endorsement upon the policy itself or by a separate instrument signed in either case by the transferor or assignor or by his duly authorised agent and attested by at least one witness, specifically setting forth the fact of transfer or assignment. S. 38(2) enacts that the transfer or assignment is not to be operative as against an insurer and is not to confer upon the transferee or assignee, or his legal representative, any right to sue for the amount of such policy or the money secured hereby until a notice in writing of the transfer or assignment together with either the said endorsement or instrument

itself or a copy thereof certified to be correct by both the transferor and transferee or their duly authorised agent has been delivered to the insurer. On a valid assignment the assignee becomes entitled to all the benefits under the contract and can sue the insurer under the contract in his own name.

#### **Payment of Claims :**

Where under a life insurance policy, the amount insured is payable only on the death of the assured, the amount may be recovered by the executor of the assured where he died leaving a will and otherwise by his administrator or legal representative. An administrator means a person to whom letters of administration have been granted by a competent court authorising him to administer the estate of a deceased person who has died without leaving a will. Under the Indian Succession Act all dues payable to a deceased dying intestate can be collected by his administrator alone. But S 212 of the Succession Act relieves a Hindu or a Mahomedian heir amongst others of the necessity of obtaining letters of administration to establish his claim to any part of the property of an intestate. It seems, therefore, that the heirs of a Hindu or Mahomedian assured can collect the insurance money falling due on his death without obtaining letters of administration. It also seems that heirs of assured can collect the insured amount without obtaining a succession certificate for under S 3 of the Indian Succession Act a succession certificate is only necessary to collect debts due to the deceased at the time of his death. It follows that the debt must also be ascertained at the death of the deceased. It has been held in Charunla Das V Jyotish Chandra<sup>1</sup>, that the amount insured payable on the death of an assured is neither ascertained, nor is it a debt due to the deceased at the time of his death. But it has been held in Ashutosh Ghose vs Pratap Chandra Banerjee<sup>2</sup> that where an insurance policy stipulates that the money due under the policy will only be paid to the "assured or his executors, administrators, or assignee" the money can only be recovered by the assured's executor where he dies leaving a will, or by his administrator where he dies intestate or by his assignee. Where the policy has been assigned by the assured the only person who can recover the

<sup>1</sup> 33 Ind. Cas. 157

<sup>2</sup> 40 C.W.N. 1242.

amount insured is the assignee and the executor or administrator of the assured has no claim to the same. Where the amount insured becomes payable before the death of the assured at a specified time as in an endowment policy and the assured remains alive at such time the amount is to be paid to the assured unless he has assigned the policy to somebody else.

In cases of life assurance policies where the amount insured becomes payable on the death of the assured the liability of the insurer arises only on the death of the assured. On his death the person or persons entitled to the insurance money has to prefer a claim to the insurer usually in one of the claims forms of the insurer with sufficient proofs of the death of the assured. The insurance company pays the money to the claimant on being satisfied of the death of the assured and of the rights of the claimant to the insurance money.

#### Surrender Value :

Prior to the Insurance Act, 1938, most policies contained a stipulation that the non-payment of any premium due by assured would entitle the insurance company to forfeit all previous payments of premium and render the policy void. But by S. 113 of the Insurance Act, 1938 such stipulation is no longer possible. S. 113 provides that if under a policy of life insurance, a definite number of premiums is payable, the policy will acquire a guaranteed surrender value provided premiums for three consecutive years have been paid and will not lapse for non-payment of any further premium and will remain alive to the extent of the paid up value. The guaranteed surrender value is the paid up value of the policy and it is an amount bearing to the total sum assured the same proportion as the total of the premiums already paid bear to the total of the premiums payable under the policy. Thus A insures his life for 20 years for Rs. 10,000/- and the premiums payable are twenty annual instalments of Rs. 600/- each amounting to Rs. 12,000/-. A pays the premiums for three years amounting to Rs. 1800/- and makes default in paying further premium. The proportion which Rs. 1800/- bears to the total premium payable namely Rs. 12,000/- is about 1/7 of Rs. 10,000/- i.e., Rs. 1429 approximately. The policy will be kept alive as a paid up policy for Rs. 1429/- to be paid on the death of A or at specified date if so stipulated.

A policy kept alive to the extent of its paid up value will not

be entitled to any profits after the conversion of the policy into a paid up policy.

The above provision in respect of surrender value and paid up policy does not apply to—

- (a) policies in respect of which the sum assured is payable only on the happening of a contingency which may not arise, e.g. where in a fire insurance no fire takes place, or
- (b) where the paid up value will be less than Rs. 100/- or
- (c) where the parties, after the default has occurred in the payment of the premium, agree in writing to some other arrangement, or
- (d) to policies in which the surrender value is automatically applied under the terms of the contract to maintain the policy in force after its lapse through non-payment of premium

#### **Personal Accident Insurance :**

In a contract of accident insurance the insurer usually undertakes to pay a certain sum to the representatives of the assured in case of his death by accident, and a certain smaller sum to the assured in case of disablement, total or partial, and to pay a certain weekly allowance to the assured during the period he is prevented from attending his normal vocation. Accident insurance is, therefore, not a contract of indemnity in as much as it provides for the payment of a specified sum on the happening of a certain event. The insurance company cannot, therefore, claim the benefit which the assured may have against a third party arising, the accident by way of subrogation.

#### **Contract How Made :**

The contract is made as in the case of fire or life insurance by the proposal of the assured and the acceptance of the same by the insurer. As in the case of other forms of insurance, the insurer has to make certain declarations and give certain particulars and information in his proposal relating to the risk undertaken by the insurer. Such declarations, particulars or information are either warranties or representations according as they are or are not embodied in or made part of the policy. The law relating to warranties and representations as well as of concealment is the same in accident insurance as in the other forms of insurance.

**Accident :**

Accident cannot be easily defined. It generally denotes an unlooked for mishap or an untoward event which is not expected or designed<sup>1</sup> e.g. a train disaster or an aeroplane crash or a motor car collision or an injury received by a workman while tending a machine. But death or injury by ordinary or common maladies like sunstroke, or pneumonia is not to be regarded as accident<sup>2</sup>. The word accident necessarily involves some violence, casualty or *vis major* and implies something fortuitous.

**Liability of the Insurer :**

In a policy of accident insurance the insurer is liable for death or injury of the assured where the same is caused proximately *i.e.* effectively and substantially by accident. Death or injury may be caused by accident even though certain intermediate stages may intervene between the accident and death or injury. Thus where a man is knocked down by a car and one of his legs is amputated to save him, the amputation of his leg is to be regarded as caused by accident though the surgeon's lincte had intervened. So also in a policy against death by accident but excluding injury arising from natural disease, if the assured is drowned owing to his being attacked by an epileptic fit the insurers are liable because the proximate cause of death is drowning and drowning is an accident.

But the insurers may limit their liability by inserting exceptions as follows:

- (1) The insurance is against death by accident with the exception of death arising from heretic erysipelas arising within the system of the insured before, or at the time of, or following, the injury. Therefore, if death takes place from erysipelas arising some days after an accident, the insurers are not liable.
- (2) The insurance is against death the sole and immediate cause of which should be bodily injury caused by violent accidental, external and visible means. Thus if death occurs due to straining of the heart in doing any strenuous job the insurers are not liable.<sup>3</sup>

<sup>1</sup> Fenton vs Thorley & Co Ltd, (1903) A.C. 441

<sup>2</sup> Sinclair vs Maritime Passengers' Insurance Co., (1861) 3 E & I 478

<sup>3</sup> Winspear vs Accident Insurance Co., (1880) 6 Q.B.D. 42 C.A.

<sup>4</sup> Re Starr & General Accident Ass Corp (1905) 1 K.B. 387

### **Insurance Against Liability to Third Persons :**

Under a policy of insurance against liability to third parties, the insurer undertakes to indemnify the assured against any specified liability which he may incur in relation to a third party e.g. where an employer insures against his liability to pay compensation to his workmen under the Workmen's Compensation Act, 1923, in case they sustain injury by accident in course of employment or where a solicitor insures against any loss arising from claims which might be made against him by reason of any neglect, omission or error committed by him in the conduct of any business connected with his professional work. In case of such a policy the insurers are only liable for any liability which arises as a result of some act of the assured which is not illegal. Thus a solicitor cannot recover any loss from his insurer if he sustains the same as a result of a criminal breach of trust of his client's property or of a champertous act ; otherwise it would mean encouraging illegal acts indirectly<sup>1</sup>.

### **Contract of Indemnity :**

Liability insurance is a contract of indemnity and on payment of the loss suffered by the assured the insurer is subrogated to all the rights of the assured. A policy of insurance of this nature usually contains express provisions giving to the company the conduct of any legal proceedings taken against the assured and enabling it to use the assured's name for the purpose of enforcing any order for costs, etc., or any claim or right of indemnity to which he may be entitled.

### **Different Kinds of Policy :**

A liability insurance may be of various kinds varying according to the nature of the risk insured. The most common forms of liability insurance are the (a) employer's liability insurance and (b) motor vehicles insurance. Under the former an employer covers his liability to pay compensation to his employees under the Workmen's Compensation Act or other Acts. Under the latter the owner of a motor car covers his liability to third parties arising out of accidents caused by the use of his motor car on the road.

<sup>1</sup> *Hoskuldine vs. Hogken*, (1933) 1 K.B. 822.

### **Guarantee Insurance :**

Under a policy of guarantee insurance the insurer undertakes to indemnify the assured for loss caused due to the default, negligence, fraud or misconduct of a third party which constitutes the risk. There are mainly three kinds of guarantee insurance, namely, (1) Fidelity Insurance, (2) Commercial Insurance and (3) Judicial Insurance<sup>1</sup>.

(1) *Fidelity Insurance*—Under this kind of insurance the insurer agrees to indemnify the assured, in consideration of certain payments known as premium, to the extent of the amount insured against loss arising through the fraud, dishonesty, or unfaithfulness of a third party (usually the servant or agent of the assured) standing in a fiduciary relationship (*i.e.*.. one of faith and trust) to the assured.

The insurance is generally effected for a fixed period and the amount of premium is generally payable in a certain number of annual instalments<sup>2</sup>.

(2) *Commercial Insurance*—Under this kind of insurance the insurer agrees to indemnify the assured, in consideration of a certain premium, to the extent of the amount insured against loss arising out of the breach of contract on the part of a third party who stands in a contractual and not fiduciary relationship to the assured<sup>3</sup>. Commercial insurance is of three types, namely contract, credit and title insurances :

(i) *Contract Insurance*—It is that branch of commercial insurance whereby the insurer, in consideration of a certain premium, agrees to indemnify the assured to the extent of the sum insured for loss or damage arising out the breach of contract by third parties in respect of contracts entered into by such third parties with the assured. A policy of contract insurance is commonly known as an indemnity bond and is issued to cover the obligations of persons like contractors, common carriers, warehousemen, apprentices and bankers.

(ii) *Credit Insurance*—It is a kind of commercial insurance whereby the insurer, in consideration of an agreed pre-

<sup>1</sup> Frost's Insurance, S. 1.

<sup>2</sup> Frost's Guarantee Insurance, S. 16.

<sup>3</sup> Ibid, S. 133.

mium, agrees to indemnify the assured to the extent of the sum specified for loss caused to the assured due to the insolvency of third parties to whom the assured has sold goods or merchandise on credit. It is also called 'solvency insurance' or 'insurance of debts'.

(ii) *Title Insurance*—It is an agreement whereby the insurer, in consideration of an agreed premium, agrees to indemnify the assured in a specified amount against loss which may be incurred due to defects in title to real estate in which the assured has an interest either as purchaser or lessee or otherwise.

(3) *Judicial Insurance*—Under this kind of insurance, the insurer agrees in consideration of certain payments known as premium, to indemnify the insured to the extent of the amount insured, for loss caused through the misconduct or negligence of a court officer e.g. a receiver or through the failure of a litigant or a party to any judicial proceeding to carry out his obligations and undertaking. Administration bonds furnished by executors, administrators, guardians, trustees and receivers are instances of judicial insurance.

#### **Insurance Act, 1938 :**

Prior to 1912 there was no Act in India applicable to insurance companies exclusively and Insurance Companies were governed by the Indian Companies Act 1908. In 1912 two Acts were passed namely, the Indian Life Insurance Companies Act, 1912 and the Provident Insurance Societies Act, 1912. The former applied only to life insurance companies established within or without British India, with the exception of companies carrying on business in the United Kingdom in accordance with the English Assurance Companies Act 1909. The latter applied only to provident societies in British India. With the growth of other forms of insurance in India after the war and as a result of the insistent demand of public opinion in India for the control of foreign companies mainly British which were exempt from the provisions of the two Acts, it was felt that the former Act was inadequate to meet the necessities of the situation. The Insurance Act, 1938 was, therefore, passed to remedy the situation. It applies to all insurance companies, life, marine, fire or provident. The Life Insurance Act, 1912 and the Provident Insurance Societies Act, 1912 are also repealed by this Act. It aims to prevent the

formation and continuation of mushroom companies and to enforce business being carried on sound principles and has made strict provisions in respect of registration, compulsory deposits, investments, inspection, and commission payable to agents, for the purpose. But the Insurance Act, 1938 does not affect the liability of insurance companies to comply with the provisions of the Indian Companies Act, 1913 in matters not otherwise specifically provided for by this Act—insurance companies are, therefore, governed by the Insurance Act, 1938 as well as by the Companies Act, 1913 in matters not covered by the former Act.

#### **Insurer :**

Insurer means<sup>1</sup>—

- (a) any individual or partnership or company incorporated under the law of any country other than British India, carrying on insurance business (other than a person mentioned in clause (c) below) which—
  - (i) carries on business in British India, or
  - (ii) has his or his principal business or is domiciled in British India,
- (b) any company (other than a person mentioned in clause (c) below) carrying on business of insurance, which is incorporated under the law of British India or which is a subsidiary company of any such incorporated company
- (c) any person who in British India has a standing contract with underwriters who are members of the Society of Lloyd's whereby such person is authorised within the terms of such contract to issue protection notes, cover notes, or other documents granting insurance cover to others on behalf of the underwriters, but does not include a licensed insurance agent or a provident insurance society

#### **Registration :**

No insurer is entitled, after the commencement of the Insurance Act, 1938 to begin to carry on any class of insurance business in British India without obtaining from the Superinten-

<sup>1</sup> S. 2(9) of the Insurance Act, 1938.

dent of insurance "a certificate of registration" and an insurer carrying on business at the time of the commencement of the Insurance Act must obtain such certificate of registration within three months from the commencement of the Insurance Act.

Every application for registration shall be accompanied by<sup>1</sup> :

- (a) a certified copy of the memorandum and articles of association where the applicant is a company, incorporated under the Indian Companies Act, 1913 or where the applicant is a foreign company a certified copy of the charter, statutes, deed of settlement or memorandum and articles or other instrument constituting or defining the constitution of the insurer, and if the instrument is not written in English, a certified translation thereof, or in the case of any other insurer a certified copy of the deed of partnership or the deed of constitution of the company, as the case may be.
- (b) the name, address, and the occupation, if any, of the directors where the insurer is a company incorporated under Indian Law and in the case of foreign companies the full address of the principal office of the insurer in British India, and the names of the directors and the manager at such office and the name and address of some one or more persons resident in British India authorised to accept any notice required to be served on the insurer and in the case of an insurer who has his or his principal place of business or is domiciled in British India, the names and addresses of the proprietors and of the manager in British India;
- (c) a statement of the class or classes of insurance business done or to be done, and a statement that the amount required to be deposited under the Act has been deposited together with a certificate from the Reserve Bank of India showing the amount deposited;
- (d) where the provisions relating to the requirement of a minimum amount of working capital apply, a declaration verified by an affidavit made by the principal officer of the insurer that the provisions as to working capital have been complied with;

<sup>1</sup> The Insurance Act, 1938, S. 3(2)

- (e) in the case of an insurer having his principal place of business or domicile outside British India, a statement verified by an affidavit of the principal officer setting forth the requirements (if any) imposed by the law of his country on Indians as a condition of carrying on insurance business in his country which are not applicable to the nationals of his country;
- (f) a certified copy of the published prospectus, if any, of the standard policy forms of the insurer and statements of the assured rates, advantages, terms and conditions to be offered in connection with insurance policies together with a certificate in connection with life insurance business by an actuary that such rates, advantages, terms and conditions are workable and sound.

Provided that in the case of marine, accident and miscellaneous insurance business other than workmen's compensation and motor car insurance, the above requirements regarding prospectus, forms and statements shall be complied with only in so far as the prospectus, forms and statements may be available; and

(g) the prescribed fee of Rs. 100/- for each class of insurance.

The Superintendent of Insurance shall, on being satisfied that the applicant has fulfilled all the requirements of the Act, grant the insurer a certificate of registration<sup>1</sup>

#### **Cancellation and Withholding of Registration :**

The Superintendent of Insurance must withhold registration or cancel the same if already made in the following cases :-

- (a) Where the insurer is a foreign company having its principal place of business or domicile outside British India and the Superintendent of Insurance is satisfied that in the country of its principal business or domicile Indians are debarred from carrying on the business of insurance; or
- (b) Where the same requirements are imposed on such foreign companies by the Central Government as those imposed on Indian Companies by the law of the place where such foreign Companies have their principal business or domicile and such foreign companies fail to satisfy them; or

<sup>1</sup> The Insurance Act, 1938, S 3(6).

(c) Where the insurer fails to deposit the amount required by the Act with the Reserve Bank of India.

If the Superintendent of Insurance cancels or withholding the grant of the certificate of registration to an insurer he must give a notice of his decision to the insurer in writing and the decision shall become effective on the date specified by him in the notice which must not be less than one month or more than two months from the date of the receipt of the notice<sup>1</sup>.

An order of the Superintendent of Insurance cancelling or withholding registration may be appealed against to the court having jurisdiction<sup>2</sup>.

#### **Restriction of Name of Insurer :**

The Superintendent of Insurance must not register an insurer by a name identical with that by which an insurer in existence is already registered, or so nearly resembling that name as to be calculated to deceive except when the insurer in existence is in the course of being dissolved and signifies his consent to the Superintendent of Insurance<sup>3</sup>. It seems that "except when the insurer in existence is in the course of being dissolved and signifies his consent" contemplates that an identical or similar name can be used in two cases *viz.*, either when the prior insurer is being dissolved or when he signifies his consent, and the word "and" should be construed as "or."

If, however, by inadvertance or otherwise an insurer is registered by a name which is identical with or so similar to that of an insurer already in existence as would be calculated to deceive the Superintendent of Insurance may on the application of the second mentioned insurer call upon the first mentioned insurer to change his name within a specified time and on being thus called upon the first mentioned insurer must change his name within the time fixed<sup>4</sup>.

The restriction regarding the use of names as mentioned above does not apply to any insurer carrying on business before the 27th of January, 1937, under the Indian Life Assurance Companies Act, 1912<sup>5</sup>.

<sup>1</sup> The Insurance Act, 1938, S. 3 (5).

<sup>2</sup> Ibid, S. 110 (1) (a).

<sup>3</sup> Ibid, S. 5 (1).

<sup>4</sup> Ibid, S. 5 (2).

<sup>5</sup> Ibid, S. 5 (3).

### **Requirements as to Capital :**

No insurer incorporated after, or who commenced carrying on the business of life insurance in British India, whether solely or in common with any other business, after the 26th day of January, 1937 shall be registered unless he has as working capital a net sum of not less than Rs 50,000/- exclusive of the deposit to be made prior to registration under the Act and also exclusive in the case of a company of any sums payable as preliminary expenses in the formation of the company. This provision is intended to arrest the growth of mushroom and invisible Companies<sup>1</sup>.

### **Requirements as to Deposit :**

Every insurer excepting one who is authorized to grant insurance cover to others under a standing contract with and on behalf of underwriters of the Society of Lloyds, must deposit in one of the offices of the Reserve Bank of India, for and on behalf of the Central Government cash or approved securities, estimated at the market value on the day of the deposit the amounts specified below.

- (a) Where the business done or to be done is life insurance only Rs 7,11,00/-
- (b) Where the business done or to be done is fire insurance only Rs 1,50,000/-
- (c) Where the business done or to be done is marine insurance only Rs 1,50,000/-
- (d) Where the business done or to be done is accident and miscellaneous insurance including Workmen's compensation and motor car Insurance Rs 1,50,000/-
- (e) Where the business done or to be done includes life and any one of the three classes specified in clauses (b), (c), and (d) Rs 3,50,000/- of which Rs 2,00,000/- shall be the deposit for life insurance business
- (f) Where the business done or to be done includes life insurance and any two of the three classes specified in clauses (b), (c) and (d), Rs 4,00,000/- of which Rs 2,00,000 shall be the deposit for life insurance business

- (g) Where the business done or to be done includes life insurance and all the classes specified in clauses (b), (c), and (d), Rs. 4,50,000/- of which Rs. 2,00,000/- shall be the deposit for life insurance business.
- (h) Where the business done or to be done does not include life insurance but any two of other classes, Rs. 2,50,000/-.
- (i) Where the business done or to be done does not include life insurance but includes all the other classes, Rs. 3,50,000/-.
- (j) Where the business done or to be done is marine insurance relating to country craft or its cargo, Rs. 10,000/-.

For insurers having contracts with underwriters of the Society of Lloyds, the requirement is that they have to deposit one and half times the deposit for each class of insurance business as specified above.

An insurance company, incorporated in India under the Indian Companies Act, 1913 and an insurer having his or her principal business or domicile in India and an insurer incorporated or domiciled in the United Kingdom, incorporated or carrying on business before the 27th day of January, 1937 may, where its business is life insurance only, make the deposit in not more than ten instalments, of which the first must not be less than one fourth of the total amount of the deposit, and be paid before the application for registration is made, the second must be not less than one ninth of the balance of the deposit and be paid before 1st January 1939 and the subsequent instalments must be not less than the second one and be paid before 1st January of each succeeding year<sup>1</sup>. But where the business of such insurers is not only life but also other forms of insurance or other forms of insurance excepting life the deposit may be made in not more than seven instalments, of which the first must be of the same amount and in the same manner as in the previous case, the second must be not less than one sixth of the balance of the deposit and be paid on the same date as in the previous case and the subsequent instalments must be not less than the second and be paid

**Time and manner of payment of deposit**

<sup>1</sup> The Insurance Act, 1938, S 7 (3).

on the same date and in the same manner as in the previous case.<sup>1</sup>

In the case of such insurers where they were neither incorporated before nor carrying on business before the 27th of January, 1937, the deposit may be made in instalments of not less than one fourth the total amount before the application for registration is made, not less than one third the balance before the expiry of one year from the commencement of business in British India, and not less than one half of the residue before the expiry of two years from the commencement of business in British India and the balance before the expiry of three years from the commencement of business in British India.

In case of insurers other than those referred to above incorporated or carrying on business before 27th January, 1937, the deposit must be made in two instalments, of which the first shall be not less than one half of the total amount of the deposit and be paid before the application for registration has been made, and the second must be made before the expiry of one year from the date of registration.<sup>2</sup> Where such insurers were neither incorporated nor carrying on business before 27th January, 1937 the deposit must be made in full before the application for registration is made.<sup>3</sup>

An insurer must not undertake new classes of business other than those for which he is liable to make deposit, until the deposit for which he is liable has been made in full.<sup>4</sup>

If any part of the deposit made under the Act is used in the discharge of any liability of the insurer, the insurer must deposit such additional sum as would cover the deficiency and the insurer shall be deemed to have failed to comply with the requirements of the Act unless the deficiency is supplied within two months from the date when the deposit or any part thereof is so used for the discharge of liabilities.<sup>5</sup>

#### **Reservation of Deposits :**

The deposit which is made by every insurer is to be deemed

<sup>1</sup> Ibid, S. 7 (3).

<sup>2</sup> Insurance Act, 1938, S. 7 (4)

<sup>3</sup> Ibid, S. 7 (5).

<sup>4</sup> Ibid, S. 7 (6).

<sup>5</sup> Ibid, S. 7 (10).

to be part of the assets of the insurer. But the insurer cannot deal with it by way of transfer, assignment or charge or use it for the discharge of any of his liabilities except those arising out of policies of insurance issued by him so long any of such liabilities remain undischarged. It is also not liable to attachment in execution of any decree except a decree obtained by a policyholder of the insurer in respect of a debt due upon a policy which debt the policyholder has failed to realise in any other way. The deposit made by an insurer in respect of life insurance business is not available for the discharge of any liability of the insurer excepting those arising out of policies of insurance issued by him.<sup>1</sup>

#### **Refund of Deposits :**

Where an insurer ceases to carry on in British India any insurance business or any class of insurance business in respect of which a deposit has been made under the Act and his liabilities in respect of his insurance business or of that branch of insurance business have been satisfied or are otherwise provided for, the court may, on the application of the insurer, order the return of the whole of the deposit in case the insurer has stopped all business or so much of it as does not relate to the classes of insurance which he continues to carry on in case the insurer ceases to do a particular class of insurance only and confirms other classes.<sup>2</sup>

#### **Separation of Account and Funds :**

Where an insurer carries on different classes of insurance business e.g., life, marine or fire, he must keep a separate account of all receipts and payments in respect of each such class of insurance business.<sup>3</sup> If the insurer carries on life insurance business along with other classes, the excess of receipts over payments in respect of such business must be carried to and form a separate fund called the 'life insurance fund' and the deposit made by the insurer in respect of life insurance business is to form a part of such fund.<sup>4</sup> The life insurance fund is to be as absolutely the security of the life policy-holders as though it belonged to an insurer carrying on no other business than life insurance business.

<sup>1</sup> Insurance Act, 1938, S. 7. (4).

<sup>2</sup> Ibid, S. 9.

<sup>3</sup> Ibid, S. 10 (1).

<sup>4</sup> Ibid, S. 10 (2).

and will not be liable for any liability of the insurer other than those connected with his life insurance business.<sup>1</sup>

#### **Accounts, Balance Sheet ; Profit and Loss and Revenue Account :**

Every insurer, in the case of an Indian company incorporated under Indian law or an insurer having his or its principal place of business or domicile in British India in respect of all insurance business transacted by him and in the case of any other insurer in respect of the insurance business transacted by him in India must at expiration of each calendar year prepare with reference to that year.<sup>2</sup>—

- (a) a balance sheet in the form set forth in part II of the first schedule to the Act and in accordance with the regulations contained in part I of that schedule. The form and regulations are set out below. The requirements of a balance sheet will appear from the regulations.
- (b) a profit and loss account in the forms set out in part II of the second schedule to the Act and in accordance with the regulations contained in part I of that schedule except where the insurer carries on only life insurance or fire insurance or marine insurance business. The forms and regulations are set out below. The requirements of a profit and loss account will appear from the regulations.
- (c) a revenue account in the form or forms set forth in part II of the Third schedule to the Act and in accordance with the regulations contained in part I of that schedule. The requirements of a revenue account will appear from the regulations.

Where the insurer is a company incorporated in India the accounts and statements referred to above should be signed in accordance with the provisions of the Indian Companies Act, 1913. But in the case of a foreign company the statements and accounts should be signed by the chairman, if any, and two directors and the principal officer of the company and in the case

<sup>1</sup> Ibid, S. 10 (3).

<sup>2</sup> Insurance Act, 1938, S. (1).

of a partnership firm by two partners of the firm or in the case of a single ownership concern by the insurer himself. The accounts and statements must be accompanied by a statement containing the names and descriptions of the persons in charge of the management of the business during the period to which such accounts and statements refer and by a report by such persons on the affairs of the business during that period.

### THE FIRST SCHEDULE

(See section 11.)

*Regulations and Forms for the preparation of Balance Sheet*

#### PART I

##### *Regulations*

1 The balance sheet required to be prepared in respect of every class of business carried on by an insurer is in the form in which it is set out in Part II of this Schedule (Form A) appropriate to a case where the insurer maintains a separate fund in respect of life insurance business.

2 The balance sheet of life insurance business shall be prepared as a separate document. The balance sheet of any class of business may be prepared as a separate document instead of being incorporated by the addition of columns and headings in the general balance sheet but the totals of each such separate balance sheet (showing the total assets of the class of business, the balance at the credit of the life insurance fund or other separate fund or account, the amount of shareholders' undivided profits, and outstanding liabilities) must in any case be incorporated in the general balance sheet.

3 If any combined balance sheet is for any purpose issued by an insurer, it shall be in accordance with the Form set out in this Schedule, and there shall not be included among the assets shown in any such combined balance sheet any amount in respect of any holding in or advance to any insurer whose assets and liabilities have been incorporated therein. Every combined balance sheet must show clearly on the face thereof that it is a combined balance sheet and must set out fully the name of every insurer whose assets and liabilities have been incorporated therein; if the assets and liabilities of any person not being an insurer are included in a combined balance sheet the fact must be stated thereon.

4 Where any guarantee has been given by an insurer (otherwise than in the ordinary course of its insurance business) in respect of the policies of any other insurer, the balance sheet of the insurer by whom the guarantee was given must show clearly the name of every insurer whose policies have been so guaranteed and the extent of the guarantee.

Provided that this regulation shall not apply where a combined balance sheet is issued incorporating the assets and liabilities of the insurer whose policies are guaranteed.

5. Where any part of the assets of an insurer is deposited in any place outside British India as security for the owners of policies issued in that place, the balance-sheet shall state that part of the assets has been so deposited, and, if any such part forms part of the life insurance fund, shall show the amount thereof and the place where it is deposited. Where any combined balance-sheet is issued by an insurer for any purpose, the information required by this regulation shall be shown in the aggregate in respect of all the insurers whose assets and liabilities have been incorporated in the balance sheet.

6. There shall be appended to the balance-sheet a statement in Form AA as set out in Part II of this Schedule showing the market value and the book value of the assets in India.

7. Every balance-sheet shall contain the following certificates, namely :—

(a) a certificate signed by the same persons as are required by this Act to sign the balance-sheet explaining how the values as shown in the balance-sheet of the Investments in Stocks and Shares have been arrived at, and how the market value thereof has been ascertained for the purpose of comparison with the values so shown ;

(b) a certificate signed by the same persons as are required by this Act to sign the balance-sheet and signed also, so far as respects the value of any items shown in the balance-sheet under the heading of "Reversions and Life Interests," by an actuary, certifying that the value of all the assets have been reviewed as at the date of the balance-sheet, and that in their belief the assets set forth in the balance-sheet are shown in the aggregate at amounts not exceeding their realizable or market value under the several headings—"Loans," "Reversions and Life Interests," "Investments," "Agent's Balances," "Outstanding Premiums," "Interest, Dividends and Rents outstanding," "Interest, Dividends and Rents accruing but not due," "Amounts due from other Persons or Bodies carrying on Insurance Business," "Sundry Debtors," "Bills Receivable," "Cash" and the several items specified under "Other Accounts" :

Provided that if the persons signing the certificate are unable to certify that the assets set forth in the balance-sheet are so shown as aforesaid, a full explanation of the bases upon which the values shown in the balance-sheet have been assessed shall be given in the certificate ;

(c) a certificate signed by the same persons as are required by this Act to sign the balance-sheet and by the auditor certifying that no parts of the assets of the life insurance fund has been directly or indirectly applied in contravention of the provisions of this Act relating to the application and investment of life insurance funds ; and

(d) certificates signed by the auditor (which shall be in addition to any other certificate or report which he is required by law to give with respect to the balance-sheet) certifying—  
 (i) that he has verified the cash balances and the securities

relating to the insurer's loans, reversions and life interests, and investments,

- (n) to what extent, if any, he has verified the investments and transactions relating to any trusts undertaken by the insurer as trustee, and
- (o) in the case of a combined balance sheet, that he has audited the balance sheet and accounts of every insurer whose assets and liabilities are incorporated therein, or that any such balance sheet and accounts which have not been audited by him have been certified by independent auditors. The said certificate shall contain a reference to such reservations, if any, as may have been made by any auditor upon any report or certificate given by him with respect to the balance sheet and accounts of any insurer whose assets and liabilities are incorporated in the combined balance sheet.

8 If the values shown in the balance sheet in respect of 'Holdings in Subsidiary Companies' or 'House property (i) in India (ii) out of India' have been increased since the last previous balance sheet, the certificate required by paragraph (b) of the last foregoing regulation shall state the amount of every increase not solely due to the cost of subsequent additions or, as respects holdings in controlled companies, to increased profits, and shall contain an explanation of the reason therefor.

9 For the purposes of this Schedule the following expressions have the meanings hereby respectively assigned to them, namely —

- (a) "combined balance sheet" includes any combined statement made by an insurer of assets and liabilities in the form of a balance sheet which includes the assets and liabilities of any other insurer, and
- (b) "market value" means as respects any asset the market value thereof as ascertained from published market quotations or, if there be no such value, its fair value as between a willing buyer and a willing seller.

PART II.

FORMS.

FORM A

*Form of Balance-sheet*

Balance-sheet of 19

Life and Annuity Business	Other Classes of Business	Total	Life and Annuity Business	Other Business	Total
(1)	(2)*	—	(1)	(2)*	—
Rs. & P.	Rs. & P.	Rs.	Rs. & P.	Rs. & P.	Rs. & P.
Shareholders' Capital (each class to be stated separately)			Loans.		
Authorised:			On Mortgages of property within British India		
Shares of Rs each Rs			On Mortgages of property outside British India		
Subscribed:			On Security of municipal and other public rates		
Shares of Rs each Rs			On Stocks and Shares		
Called up:			On Insurer's policies within their surrender value		
Shares of Rs each Rs			On Personal security		
Less Unpaid calls Rs			To Subsidiary Companies (other than Reversionary) (f)		
Reserve or Contingency Accounts (a):					
Investment Reserve A/c					

<u>Profit and Loss Appropriation Account Balance ..</u>	<u>Reversions &amp; Life Interests:</u>
<u>Balances of Funds and Accounts:</u>	<u>Reversions and Life Interests purchased ..</u>
<u>Life Insurance Fund ..</u>	<u>Loans on Reversions and Life Interests .. ..</u>
<u>Fire Insurance Business Account .. .. ..</u>	<u>Debentures and Debenture Stocks of Subsidiary Reversionary Companies (f)</u>
<u>Marine Insurance Business Account .. .. ..</u>	<u>Ordinary Stocks and Shares of Subsidiary Reversionary Companies (f) ..</u>
<u>Accident and Miscellaneous Insurance Business A/c.</u>	<u>Loans to Subsidiary Reversionary Companies (f)</u>
<u>Other accounts, if any (to be specified) (i) .. ..</u>	<u>Investments:</u>
<u>Pension or Superannuation Accounts (b) .. ..</u>	<u>Deposit with the Reserve Bank of India (Securities to be specified) .. ..</u>
<u>Debenture Stock per cent.</u>	<u>Indian Government Securities .. ..</u>
<u>Loans and Advances (c) ..</u>	<u>Provincial Government Securities .. ..</u>
<u>Bills Payable (c) .. ..</u>	<u>British, British Colonial and British Dominion Government Securities .. ..</u>
<u>Estimated Liability in respect of outstanding claims, whether due or intimated (d) .. .. ..</u>	<u>Foreign Government Securities .. ..</u>
<u>Annuities due and unpaid (d) .. .. ..</u>	<u>Indian Municipal Securities .. ..</u>
<u>Outstanding Dividends ..</u>	<u>British and Colonial Securities .. ..</u>
<u>Amounts due to Other Persons or Bodies carrying on Insurance Business (c)</u>	<u>Foreign Securities ..</u>
<u>Sundry Creditors (including outstanding and</u>	<u>Bonds, Debentures, Stocks ..</u>

FORM A—contd.

	Life and Annuity Business (1)	Other Business (2)*	Total		Life and Annuity Business (1)	Other Business (2)*	Total
accruing expenses and Taxes) (c)	Rs A P	Rs A P	Rs A P	and other Securities whereon Interest is gua ranteed by the Indian Government or a Provin cial Government	Rs A P	Rs A P	Rs A P
Other sums owing by the insurer (particulars to be given) (c)				Bonds, Debentures, Stocks and other Securities whereon Interest is gua ranteed by the British or any Colonial Govern ment			
Contingent Liabilities (to be specified) (c)				Bonds, Debentures, Stocks and other Securities whereon Interest is gua ranteed by any Foreign Government			
Rs —				Debentures of any railway out of India			
				Preference or guaranteed Shares of any railway in India			

Preference or guaranteed Shares of any railway out of India .. ..	
Railway Ordinary Stocks (i) in India (ii) out of India ..	
Other Debentures and Debenture Stock of Companies incorporated (i) in India (ii) out of India ..	
Other guaranteed and Preference Stocks and Shares of Companies incorporated (i) in India (ii) out of India .. ..	
Other Ordinary Stocks and Shares of Companies incorporated (i) in India (ii) out of India .. ..	
Holdings in Subsidiary Companies (f) .. ..	
House property (i) in India (ii) out of India .. ..	
Freehold and Leasehold ground rents and rent charges .. ..	
Agent's Balances .. ..	
Outstanding Premiums (g)	
Interest, Dividends and Rents outstanding (d) ..	
Carried over .. ..	

FORM A—contd.

Life and Annuity Business.	Other Class of Business.	Total.	Life and Annuity Business.	Other Class of Business.	Total.
(1)	(2)*		(1)	(2)*	
Rs. A. P.	Rs. A. P.	Rs. A. P.	Rs. A. P.	Rs. A. P.	Rs. A. P.
Brought forward ..					
Interest, Dividends and					
Rents accruing but not					
due (d) .. .. ..					
Amounts due from Other					
Persons or Bodies carry-					
ing on Insurance Busi-					
ness (h) .. .. ..					
Sundry Debtors (i) .. ..					
Bills Receivable .. ..					
Cash:					
At Bankers on Deposit					
Account .. .. ..					
At Bankers on Current Ac-					
count and in hand .. ..					
At Call and Short Notice (j)					
Other Accounts (to be spe-					
cified (k) .. .. ..					

\* Assets and Liabilities, Shareholders' Capital and Reserves, not allocated to any class of business specified in column (1) must be shown in column (2).

*Notes.*

- (a) The Reserves or Contingency Accounts must be separately stated.
- (b) If the insurer has not full and unrestricted control of the assets constituting the Pension or Superannuation Accounts, either those Accounts and the assets and liabilities relating thereto must be omitted from the balance-sheet or the assets of which the insurer has not such control must be clearly indicated on the face of the balance-sheet.
- (c) If the insurer has deposited security as cover in respect of any of these items, the amount and nature of the securities so deposited must be clearly indicated on the face of the balance-sheet.
- (d) These items are or have been included in the corresponding items in the Revenue or Profit and Loss Account. Outstanding and accruing interest, dividends and rents must be shown after deduction of income-tax or the income-tax must be provided for amongst the liabilities on the other side of the balance-sheet.
- (e) Such items as amount of liability in respect of bills discounted, uncalled capital of subsidiary companies, uncalled capital of other investments, etc., must either be shown in their several categories under the heading "Contingent Liabilities" or the appropriate items on the assets side must be set out in such detail as will clearly indicate the amount of the uncalled capital.
- (f) As respects life and annuity business full particulars of holdings in and loans to subsidiary companies must be stated, giving the name of each company, the number and description of each class of shares held, the amounts paid up thereon, and the value at which the holdings in each company stand in the balance-sheet.
- (g) Either this item must be shown net or the commission must be provided for amongst the liabilities on the other side of the balance-sheet.
- (h) The aggregate amount owing by a subsidiary company or subsidiary companies is to be shown separately from all other assets and the aggregate amount owing to a subsidiary company or subsidiary companies is to be shown separately from all other liabilities.
- (i) Amounts due from directors and officers must be shown separately.
- (j) No amounts must be entered under this heading unless fully secured. If not fully secured, the amounts must be included under the heading "Sundry Debtor."
- (k) Under this heading must be included such items as the following, which must be shown under separate heading suitably described: office furniture, goodwill, preliminary, formation and organization expenses, development expenditure account, discount on debentures issued, other expenditure carried forward to be written off in future years, balance being loss on Profit and Loss Appropriation Accounts, etc. The amounts included in the balance-sheet must not be in excess of cost.
- (l) Under the head "Other accounts, if any (to be specified)" on the left hand side, fines realized from the staff and their contribution towards the provident fund, if any, should be shown under a suitable sub-head.

## FORM AA

Classified Summary of the Indian Assets of the  
Company on

19

Class of Asset	Book value as per (b) below	Market value as per (b) below	Remarks as per (c) below
	Rs	Rs	
(1) Government of India Securities			
(2) Indian Provincial Government Securities			
(3) Indian Municipal and Government Trust Securities including Debentures			
(4) Debentures of Indian Railways			
(5) Guaranteed and Preference Shares of Indian Railways			
(6) Annuities of Indian Railways			
(7) Ordinary Shares of Railways in India			
(8) Other Debentures of concerns in India			
(9) Other Guaranteed and Preference Shares of concern in India			
(10) Other Ordinary Shares of concern in India			
(11) Loans on the Company's policies effected in India and within the surrender value			
(12) Loans on Mortgage of property in India			
(13) Loans on Personal Security to persons domiciled and resident in India			
(14) Other loans granted in India (particulars to be stated)			
(15) Land and House Property in India			
(16) Cash on Deposit in banks in India			
(17) Cash in Hand and on current account in banks in India			
(18) Agents' balances and outstanding premiums			

FORM AA.—*Contd.*

Class of Asset.	Book value as per (a) below. Rs.	Market-value as per (b) below. Rs.	Remarks as per (c) below.
(19) Interest, dividends and rents either outstanding or accrued but not due			
(20) Other assets in India (to be specified)			

The statement shall show—

- (a) the value for which credit is taken in the balance-sheet for each of the above mentioned classes of assets,
- (b) the market value of such of the above mentioned classes of assets as has been ascertained from published quotations after deduction of accrued interest included in market prices in those cases where accrued interest is included elsewhere in the balance-sheet,
- (c) how the value of such of the above mentioned classes of assets as has not been ascertained from published quotations has been arrived at, and
- (d) the rates of exchange at which the values of the assets other than in rupee currency have been converted into rupees.

The market values need not be shown separately where they are not less than the book values and a certificate to that effect is appended to the statement.

No amounts on account of any of the following items may be entered into the statement :—

Goodwill

Preliminary, formation, organisation or development expenses.

Commission or discount on shares or debentures issued.

Committed Commission.

Expenditure carried forward to be written off in future years.

### THE SECOND SCHEDULE.

(See section 11.)

*Regulations and Forms for the preparation of Profit and Loss Accounts.*

#### PART I.

##### *Regulations.*

1. The items on the income side of the Profit and Loss Account and Profit and Loss Appropriation Account must relate to income whether actually received or not, and the items on the expenditure side must relate to expenditure whether actually paid or not.

2. Deductions from Interest, Dividends and Rents to be shown in respect of income-tax must include all amounts in respect of British Indian income-tax whether or not it has been or is to be deducted at source or paid direct.

3. The Interest, Dividends and Rents, *less* income-tax thereon shown in the Revenue Accounts for any classes of business other than life insurance business, including annuity business may, if the insurer so desires, be included with the corresponding items in the Profit and Loss Account.

**PART II**  
**FORM B**

*Form of Profit and Loss Account*  
 Profit and Loss Account of for the year ended 19

Rs. A. P.

British India Taxes on the Insurer's Profits (not applicable to any particular Fund or Account)	Interest, Dividends and Rents (not applicable to any particular Fund or Account) Rs.
Expenses of Management (not applicable to any particular Fund or Account)*	Less — Income tax thereon Rs.
Loss on Realisation of Investments (not charged to Reserves of any particular Fund or Account)	Profit on realisation of Investment (not credited to Reserves or any particular Fund or Account)
Depreciation of Investments (not charged to Reserves or any particular Fund or Account)	Appreciation of Investments (not credited to Reserve or any particular Fund or Account)
Loss transferred from Revenue Accounts (detail to be given)	Profit transferred from Revenue Accounts (detail to be given)
Other Expenditure (to be specified)	Transfer Fees
Balance for the year carried to Appropriation Account	Other Income (to be specified)
	Balance being loss for the year carried to Appropriation Account

\* If any sum has been deducted from this item and entered on the assets side of the balance sheet, the amount must be shown separately

## FORM C

*Form of Profit and Loss Appropriation Account*

Profit and Loss Appropriation Account of      for the year ended      19

Rs A. P	Rs
Balance being loss brought forward from last year	Balance brought forward from last year      Rs.
Balance being loss for the year brought from Profit and Loss Account (as in Form B)	Less—Dividends since paid in respect of last year (to be specified and if 'free of tax' to be so stated)*      Rs
Dividends paid during the year on account of the current year (to be specified and if 'free of tax' to be so stated)	
Transfers to any particular Funds or Accounts (details to be given)	Balance for the year brought from Profit and Loss Account (as in Form B)
Balance at end of the year, shown in the Balance-Sheet	Balance being loss at end of the year as shown in the Balance Sheet

\* Note.—This item may be shown on the other side of the account if preferred.

## THE THIRD SCHEDULE.

(See section 11.)

*Regulations and Forms for the preparation of Revenue Accounts.*

## PART I.

*Regulations.*

1. Form D is, as set out in Part II of this Schedule, appropriate for life insurance business, but a separate revenue account must be prepared for every class of business in respect of which the insurer is required to maintain a separate account.

2. Form E is, as set out in Part II of this Schedule, appropriate for fire insurance business. A separate revenue account in the same form must be prepared for accident and miscellaneous insurance including workmen's compensation and motor car insurance. Form F is, as set out in Part II of this Schedule, appropriate for marine insurance business.

3. If any combined revenue account is for any purpose issued by an insurer it must be in accordance with the forms specified in this Schedule and must clearly show on the face thereof that it is a combined revenue account, and must set out fully the name of every insurer required to make separate returns under this Act whose revenue and expenditure have been included therein; if the revenue and expenditure of any person not being an insurer are included in a combined revenue account, the fact must be stated thereon.

4. The items on the income side of the revenue account must relate to income whether actually received or not, and the items on the expenditure side must relate to expenditure whether actually paid or not.

5. Re-insurance premiums, whether on business ceded or accepted, are to be brought into account gross (*i.e.*, before deducting commissions) under the head of premiums.

6. As respects life insurance business the following statements shall be furnished to the Superintendent of Insurance every year showing details provided for in a Form pertaining thereto:—

- (A) A statement in form DD as set forth in Part II of this Schedule.
- (B) A statement in form DDD as set forth in Part II of this Schedule
- (C) A statement in form DDDD as set forth in Part II of this Schedule.

7. The following information shall be supplied in addition to the revenue account, namely, the gross premium written in India for life, fire, marine and accident and miscellaneous insurance business.

8. Any office premises which form part of the assets of a life insurance fund must be treated as an interest earning investment, and accordingly, in the revenue account for life insurance business a fair rent for the premises must be included under the heading "Interest, Dividends and Rents" and in the revenue account for every class of business for which the premises are used, proper charges for the use thereof must be included under the heading "Expenses of Management."

9. Where an insurer carries on the business of life insurance in conjunction with any other class of insurance business the expenses of management charged to the life insurance revenue account must not include more than a reasonable proportion of the common expenses and in particular no such account must be charged with more than a fair sum for the use of any office premises having regard to the income from the various classes of business carried on and to the extent to which the premises are used for the purposes of each class of business.

10. Deductions from Interest, Dividends and Rents in respect of income-tax must include all income tax charged on such income whether or not it has been or is to be deducted at source or paid direct; the income-tax to be shown as so deducted in the life insurance Revenue Account is British Indian, United Kingdom, Foreign and Dominion income tax, but the income-tax to be shown as deducted in Revenue Accounts of any other classes of business is British Indian income-tax only.

PART II  
FORMS.  
FORM D

Form of Revenue Accounts applicable to Life Insurance Business

	Business within India	Business out of India (s)	Total		Business within India	Business out of India (s)	Total
	Rs.	Rs.	Rs.		Rs.	Rs.	Rs. A. P.
Claims under Policies (including provision for claims due or estimated) less Re-insurance				Balance of Fund at the beginning of the year			
By death				Premiums less Returnances—			
By maturity				(i) First year premium			
Annuities, less Re-insurances				(ii) Renewal premiums			
Surrenders (including Surrenders of Bonus), less Re-insurance				(iii) Single premiums			
Bonuses in cash, less Re-insurance				Consideration for Annuities granted, less Re-insurances (c)			Rs.
Bonuses in Reduction of Premium, less Re-insurance				Interest Dividends and Rent			
Commission (less that on Re-insurance)				Less—Income thereon (d)			Rs.
				Registration Fees			
				Other Income (to be specified) (e)			

Expenses of Management	Loss transferred to Profit and Loss Account
(b)—	Transferred from Appropriation Account
1 Commission and allowances	
2 Salaries, etc (other than to agents and those contained in item No 1)	
3 Travelling expenses	
4 Directors fees	
5 Auditors' fees	
6 Law charges	
7 Advertisements	
8 Printing and Stationery	
9 Other expenses of management (amounts to be specified)	
10 Other payments (amounts to be specified)	
11 Rents for offices belonging to and occupied by the insurer	
12 Rents of other offices occupied by the insurer	
Bad Debts	
United Kingdom British	
Indian Dominion and Foreign Taxes	
Other Expenditure (to be specified)	
Profit transferred to Profit and Loss Account	
Balance of Fund at the end of the year as shown in the Balance Sheet	

*Notes.*

- (a) In the case of an insurer having his head office in British India, these columns apply only to business the premiums in respect of which are payable outside India.
- (b) If any sum has been deducted from this item and entered on the assets side of the balance-sheet, the amount so deducted must be shown separately. Under this item the salary paid to the managing agent or managing director shall be shown separately from the total amount paid as salaries to the remaining staff.
- (c) All single premiums for annuities, whether immediate or deferred, must be included under this heading.
- (d) British Indian, United Kingdom, Foreign and Dominion income-tax on Interest Dividends and Rents must be shown under this heading, less any rebates of income-tax recovered from the revenue authorities in respect of expenses of management. The separate heading on the other side of the account is for United Kingdom, British India, Foreign and Dominion taxes, other than those shown under this item.
- (e) Under the head "Other Income" fines, if any, realised from the staff must be shown separately. All the amounts received by the insurer directly or indirectly whether from his head office or from any other source outside British India shall also be shown separately in the revenue account except such sums as properly appertain to the capital account.
- (f) In the case of an insurer having his principal place of business outside British India the expenses of management for business out of India and total business need not be split up into the several sub-heads, if they are not so split up in his own country.

**Audit :**

The balance sheet, profit and loss account, Revenue Account and profit and loss appropriation account of every Indian Company or every insurer having his place of business or domicile in British India, in respect of all insurance business transacted by it or him, and of every non-Indian insurer, in respect of the insurance business transacted by him in India, must be audited annually by an auditor unless in the case of an Indian Company, it is already subject to audit under the Indian Companies Act, 1913. The auditor is to have the same rights and liabilities as provided for in S. 145 of the Indian Companies Act<sup>1</sup>.

**Actuarial Report and Abstract :**

Every insurer carrying on life insurance business must, once at least in every five years, cause an investigation to be made by an actuary into the financial condition of the life insurance business carried on by him, including a valuation of his liabilities in respect thereto and shall cause an abstract of the report of such actuary to be made in accordance with the regulations and requirements contained in Parts I and II of the Fourth Schedule to the Act. Such abstract must be accompanied by a certificate signed by the principal officer of the insurer that full and accurate particulars of every policy under which there is a liability, actual or contingent, have been furnished to the actuary for the purpose of investigation. The valuation report of the actuary must also specify the life insurance business in force at the date. The investigation and valuation must relate to the whole of the life insurance business in the case of Indian Companies or insurers having their principal place of business or domicile in India and to the life insurance business transacted in India in the case of insurers having their principal place of business or domicile outside India.<sup>2</sup>

Every abstract prepared by the actuary must contain a certificate by the actuary that he has satisfied himself as to the accuracy of the valuations made and must show the following amongst others :—

- (i) the valuation date ;

<sup>1</sup> Insurance Act, 1938, S. 12.

<sup>2</sup> Insurance Act, 1938, S. 13.

- (ii) the general principles and full details of the methods adopted in the valuation of each of the various classes of insurance including statements as to whether the principles were determined by the instruments constituting the company or by its regulations or bye laws or how otherwise, the method by which the net premiums have been arrived at and how the ages at entry, premium terms and maturity dates have been treated and so on.
- (iii) the table of mortality used, and the rate of interest assumed in the valuation.
- (iv) the basis adopted in the distribution of profits as between the insurer and policy-holders.
- (v) the general principles adopted in the distribution of profits among policy-holders.

#### **Submission of Returns :**

The audited account and statements in balance sheet, profit and loss account and revenue account and the actuarial report and abstract referred to above must be printed and five copies thereof must be furnished as returns to the Superintendent of Insurance within six months from the end of the period to which they refer. The period may be extended by the Superintendent of Insurance in the case of the furnishing of actuarial abstract and also in the case of insurers having their principal place of business or domicile outside British India or Indian insurers doing business outside India<sup>1</sup>. Of the four copies so furnished one must be signed in the case of a company by the Chairman and two directors and by the principal officer of the company and, if the company has a managing director or managing agent, by that director or managing agent, and, in the case of a firm, by two partners of the firm, and, in the case of an insurer being an individual, by the insurer himself<sup>2</sup>.

Where an insurance company incorporated in India furnishes its accounts and balance sheet to the Superintendent of Insurance in the manner referred to above, it need not file its balance sheet with the Registrar of Joint Stock Companies of the province under S. 134 of the Indian Companies Act and it will be sufficient com-

<sup>1</sup> Insurance Act, 1938, S. 15 (1).

<sup>2</sup> Insurance Act, 1938, S. 15 (2).

pliance with the Indian Companies Act if it sends to the Registrar a copy of the accounts and balance sheet furnished to the Superintendent of Insurance.

Every insurer must also submit to the Superintendent a certified copy of every report on the affairs of the concern which is submitted to the members or policy-holders and if it is a company incorporated in India, it must also submit to the Superintendent an abstract of the proceedings of every general meeting within thirty days from the holding of the meeting to which it relates<sup>1</sup>.

#### **Requirements of Returns for Foreign Companies :**

Where a foreign insurer carrying on business in India is required by the law of the country in which he or it is constituted, incorporated or domiciled to prepare and to furnish to a public authority of that country documents of substantially the same nature as the balance sheet, profit and loss account, Revenue Account and actuarial report and abstract, such insurer is not required to prepare such accounts, statements and abstracts according to the Indian law and the provisions of the Act will be sufficiently complied with if such insurer furnishes to the Superintendent of Insurance four certified copies in the English Language of every balance sheet, account, abstract, report and statement supplied to the public authority of his or its own country according to its law within six months from the end of the period to which such documents refer together with the following statements, namely : - <sup>2</sup>.

- (a) a statement showing the assets held by the Insurer in India.
- (b) revenue account showing each class of business transacted by it in India.
- (c) an abstract of the valuation report in respect of all life insurance business transacted by the insurer in India.
- (d) A declaration in the prescribed form stating that all amounts received by the insurer have been shown in the revenue account except such sums as properly appertain to the capital account.

#### **Custody and Inspection of Documents and Supply of Copies :**

Every return furnished to the Superintendent of Insurance or

<sup>1</sup>Ibid. Ss. 18 and 19.

<sup>2</sup>Ibid. S. 20 (2).

a certified copy thereof is to be kept by the Superintendent and to be kept open for inspection ; and any person may procure a copy of any such return, or of any part thereof, on payment of a fee of six annas for every hundred words<sup>1</sup>.

Every insurer must supply within fourteen days a printed or certified copy of the accounts, statements and abstract, furnished to the Superintendent under the Act, on the application of any share-holder or Policy-holder made at any time within two years from the date on which the document was so furnished, when the insurer is constituted, incorporated or domiciled in British India and in any other case within one month of such application<sup>2</sup>.

#### **Superintendent of Insurance, his powers and duties :**

Superintendent of Insurance is the Officer, who is a qualified actuary, appointed by the Central Government to perform the duties of the Superintendent of Insurance under the Insurance Act, 1938<sup>3</sup>. The control and supervision of insurance companies by the Central Government is exercised through the Superintendent of Insurance and the machinery of Control which the Act has provided for makes the Superintendent the most important figure in the whole scheme of the Act. In fact the shadow of the Superintendent looms over every sphere of insurance companies sought to be controlled and supervised by the Act. His powers and duties may be enumerated as follows : -

(a) He grants the certificate of registration to an insurer.

The application for registration is to be made to him and he sees whether the requirements of the Act have been satisfied before he grants the certificate. He has the power to cancel or withhold registration subject to his decisions being appealed against to the Court.

(b) The certified copies, audited balance sheet, profit and loss account, revenue account and the actuarial report and abstract of every insurer is to be furnished to the Superintendent within a prescribed time. If it appears

<sup>1</sup> Insurance Act, 1938, S. 20 (1).

<sup>2</sup> Ibid, S. 20 (2).

<sup>3</sup> Ibid, S. 2 (15).

to the Superintendent that any return so furnished is inaccurate or defective in any respect, he may<sup>1</sup>

- (i) require from the insurer such further information, certified if he so directs by an auditor or actuary as he may consider necessary to correct or supplement such return;
- (ii) call upon the insurer to submit for his examination at the principal place of business of the insurer in British India any book of account, register or other document or to supply any statement which he may specify in a notice served on the insurer for the purpose;
- (iii) examine any officer of the insurer on oath in relation to the return;
- (iv) decline to accept any such return unless the deficiency has been supplied before the expiry of one month from the date on which the requisition for correcting the inaccuracy or supplying the deficiency was delivered to the insurer and on his declining to accept such return the insurer is to be deemed to have failed to comply with the provisions of the Act.

The decision of the Superintendent as regards declining to accept any return is subject to appeal to the Court<sup>2</sup>

- (c) If it appears to the Superintendent that an investigation and valuation of the business of an insurer by an actuary does not properly indicate the condition of the affairs of the insurer by reason of the faulty basis adopted in the valuation, he may, after giving notice to the insurer and giving him an opportunity to be heard, cause an investigation and valuation to be made at the expense of the insurer by an actuary appointed by the insurer for this purpose and approved by the Superintendent;
- (d) If the Superintendent has reason to believe that the interests of the policy-holders of an insurer are in danger

<sup>1</sup> Insurance Act, 1938, S. 21 (1)

<sup>2</sup> Ibid, S. 21 (2)

or that an insurer is unable to meet his obligations or has made default in complying with any of the provisions of the Act, or that an offence under the Act has been or is likely to be committed by an insurer or any of his officers or if he receives a requisition in this behalf signed by the shareholders of an insurance company not less in number than one tenth of the whole body of shareholders and holding not less than one tenth of the whole share capital or if he receives a requisition in this behalf signed by not less than fifty policyholders holding policies of life insurance that have been in force for not less than three years and are of the total value of not less than Rs 50,000 and supported by an affidavit he may after giving notice to the insurer and giving him an opportunity of being heard appoint an auditor or actuary or both not being an auditor or actuary in the employ of the insurer to investigate the affairs of the insurer or may himself make such investigation. The Superintendent may require the insurer to comply within a specified time with any direction he may issue to remedy the defects disclosed by such investigation. If the insurer fails to comply with such direction or if in result of the investigation the Superintendent is of opinion that the business of the insurer should be wound up in the interests of the Policy holder the Superintendent may after giving notice to the insurer and giving him an opportunity of being heard, apply to the court to have the business of the insurer wound up<sup>1</sup>.

- (c) The Superintendent has the power to prosecute insurers or where the insurer is a company its directors or principal officer for non-compliance with the provisions of the Act.
- (d) The Superintendent may take such steps as he may consider necessary to inspect and verify that the assets of an insurer are invested as required by the Act.

#### **Register of Policies and Claims :**

An insurer who has his principal place of business or domicile

<sup>1</sup> Insurance Act, S 33 (1), (4) and (5)

<sup>2</sup> Ibid, S 107

in British India or a company incorporated in India must, in respect of all insurance business, and an insurer incorporated or constituted outside British India must, in respect of the insurance business transacted by him in India, maintain (a) a register of policies and (b) a register of claims<sup>1</sup>. In a register or record of policies must be entered in respect of every policy issued by the insurer, the name and address of the Policy-holder, the date when the policy was effected and a record of any transfer, assignment or nomination of which the insurer has notice<sup>2</sup>. In a register or record of claims must be entered every claim made together with the date of the claim, the name and address of the claimant and the date on which the claim was discharged, or in the case of a claim which is rejected, the date of rejection and the grounds therefor<sup>3</sup>.

#### **Investments :**

Every insurer incorporated in or domiciled in India or the United Kingdom must invest and hold invested assets to the extent of fifty-five per cent of the sum of his total liabilities to the holders of life insurance policies in India, representing matured claims and claims to mature, less the amount deposited by it with the Reserve Bank of India in accordance with the provisions of the Act and the amount lent by him to policy-holders on policies of life-insurance, in the following manner<sup>4</sup>.

- (a) Twenty five per cent of such total liabilities in Government Securities, and
- (b) Thirty per cent of such total liabilities in Government securities or other approved securities or securities of or guaranteed by the Government of the United Kingdom.

But an insurer incorporated or domiciled elsewhere than in British India or the United Kingdom and an insurer incorporated in British India whose share capital to the extent of one-third is owned by, or the members of whose governing body to the extent of one-third consists of, individuals domiciled elsewhere than in British India or the United Kingdom, must invest and hold invested assets to the whole extent of the sum of his total liabilities to

<sup>1</sup> Ibid, S. 14.

<sup>2</sup> Ibid, S. 14.

<sup>3</sup> Ibid, S. 14.

<sup>4</sup> Insurance Act, 1938, S. 27 (1).

holders of life insurance policies in India on account of matured claims and claims to mature less the amount of his deposit and any amount due to him on loans granted by him on policies of life insurance, in the following manner<sup>1</sup>:—

- (a) Thirty-three and one third per cent of such total liabilities in Government securities, and
- (b) the balance of such total liabilities in Government securities or other approved securities or securities of or guaranteed by the Government of the United Kingdom.

Every insurer carrying on business at the commencement of the Act must invest his assets in the above manner within four years from the commencement of the Act<sup>2</sup>.

Every insurer other than provident society registered under the Act and carrying on the business of life insurance, is required, twice in every year, namely within fourteen days of the 30th of June and 31st of December respectively, to submit to the Superintendent of Insurance a statement certified by the principal officer of the insurer showing as at the said dates the assets held invested in accordance with the above provisions.<sup>3</sup> The Superintendent can at any time take proper steps to verify and inspect the assets invested in the manner required by the Act and the insurer must comply with all requisitions made by the Superintendent in that behalf<sup>4</sup>.

#### **Prohibition of Loans :**

No insurer can grant loans or temporary advances to (a) any director, managing agent, manager, auditor, actuary or officer of the insurer where the insurer is a company or (b) to any partner of the insurer where the insurer is a partnership or (c) to any other company or firm, excepting a banking concern in which any such director, manager, managing agent, actuary, officer or partner holds the positions of a director, manager, managing agent, actuary, officer or partner, either on hypothecation of property or on personal security or otherwise excepting where the loan or advance is given on life policies issued by the insurer to the extent of the

<sup>1</sup> Ibid. S. 27 (2).

<sup>2</sup> Insurance Act, S. 27 (3).

<sup>3</sup> Insurance Act, S. 28 (1).

<sup>4</sup> Ibid. S. 28 (2).

surrender value of such policies<sup>1</sup>. In the case of loans to such specified persons as in (a) and (b) existing at the commencement of the Act, such loans must have been repaid within one year from the commencement of the Act and in case of default such defaulting director, manager, managing agent, auditor, actuary, officer or partner shall cease to hold office on the expiry of such one year.

#### **Limitation on Employment of Managing Agents :**

The Insurance Act, 1938, prohibits the appointment of a managing agent for the conduct of the business of an insurer.<sup>2</sup> If an insurer is a company which was engaged in the business of insurance before the commencement of the Act and employed a managing agent for the conduct of its business, then such managing agent shall cease to hold office on the expiry of three years from the commencement of the Act, notwithstanding anything contained in the Indian Companies Act, 1913, or in the memorandum and articles of the insurer or in the agreement with the managing agent, and such managing agent shall not be entitled to claim any compensation from the insurer for the premature termination of his employment<sup>3</sup>. The insurer must not pay and such managing agent must not accept as remuneration more than Rs. 2000/- per month in all, including all salary, commission and other remuneration payable to the managing agent, during the three years after the commencement of the Act during which the managing agent will be able to function<sup>4</sup>.

#### **Amalgamation and Transfer of Insurance Business :**

No life insurance business excepting an insurer constituted, domiciled or incorporated outside British India, can be transferred to or amalgamated with the life insurance business of any other insurer except in accordance with a scheme prepared and sanctioned by the Court having jurisdiction over one or other of the insurers concerned in the following manner<sup>5</sup>:

- (a) The scheme must set out the agreement under which the transfer or amalgamation is proposed to be effected.

<sup>1</sup> Insurance Act, 1938, S. 29

<sup>2</sup> Insurance Act, 1938, S. 32 (1)

<sup>3</sup> Ibid, S. 32 (2).

<sup>4</sup> Insurance Act, 1938, S. 32 (3).

<sup>5</sup> Ibid, S. 35 (1).

and shall contain such further provisions as may be necessary for giving effect to the scheme.

- (b) After the scheme is prepared and before any application may be made to the Court for its sanction, notice of the intention to make the application together with a statement of the nature of the amalgamation or transfer, as the case may be, and of the reason therefor must at least two months before the application is made, be sent to the Central Government together with certified copies of the following documents—
- (i) a draft of the agreement or deed under which it is proposed to effect the amalgamation or transfer;
  - (ii) statements of the assets and liabilities of the insurers concerned in such amalgamation or transfer; and
  - (iii) the material or other reports on which the scheme was founded including a report by an independent actuary on the proposed amalgamation or transfer.

These documents are to be kept open for inspection of the members and policy holders at the principal and branch offices and the headquarters of the insurers concerned during the two months before the application is made.

- (c) After the expiry of two months the application may be made to any of the courts mentioned above. The Court if it so directs shall cause notice of the application to be sent to every holder of life policy of the insurers concerned and a statement of the nature of the amalgamation or transfer in the case may be to be published in such manner and for such period as it may direct and after hearing the directors and such Policy holders or other persons as may apply or are entitled to be heard may sanction the arrangement, if it is satisfied that no sufficient objection to the arrangement has been established.<sup>1</sup>

#### **Statements required after amalgamation or transfer:**

In the case of every amalgamation or transfer whether in accordance with the provisions of the Act which applies to Individual insurers only or otherwise, the insurer carrying on the amalgam-

<sup>1</sup> Ibid § 36

ted business or to whom the business has been transferred must, within three months from the completion of the amalgamation or transfer, furnish to the Central Government<sup>1</sup>

- (a) a certified copy of the scheme, agreement or deed under which the amalgamation or transfer has been effected, and
- (b) a declaration signed by every insurer concerned or in the case of a company by the Chairman or the principal officer that to the best of their belief every payment made or to be made to any person whatsoever on account of the amalgamation or transfer is fully set forth in the declaration, and
- (c) where the amalgamation or transfer has not been made in accordance with a scheme confirmed by the Court or where the amalgamation or transfer is between non-Indian insurers
  - (i) certified copies of statement of the assets and liabilities of the insurers concerned, and
  - (ii) certified copies of the actuarial or other reports upon which the agreement or deed was founded

#### **Assignment or transfer of Policies :**

We have dealt with this subject already under Life Insurance.

#### **Nomination by Policy-holder :**

The holder of a policy may at the time of effecting the policy or at any time before the policy matures for payment, nominate a person or persons to whom the money secured by the policy shall be paid in the event of his death. Such nomination to be valid must be either incorporated in the text of the policy itself or be made by an endorsement on the policy, communicated to the insurer and registered by him in the records relating to the policy. The insurer may charge a fee not exceeding Re 1/- for registering any such endorsement. But any such nomination may at any time before the policy matures for payment be cancelled or changed by an endorsement or further endorsement or a will as the case may be and ceases to have effect automatically on an assignment or transfer of the Policy. The nominee has no claim

<sup>1</sup> Insurance Act, 1938, S 37

to the money payable under the Policy if the policy-holder is alive when the policy matures for payment. If the nominee is not alive at the time of the death of the policy-holder, the heirs or legal representative of the policy-holder and not of the nominee becomes entitled to the insurance money<sup>1</sup>.

### Licensing of Insurance Agents :

Any person not suffering from the disqualifications mentioned below may obtain a license to act as an insurance agent for the purpose of soliciting or procuring insurance business from the Superintendent of Insurance or an officer authorised by him in this behalf on payment of a fee not exceeding Rs. 1/-<sup>2</sup>. A license issued under the provisions of the Act entitles the holder to act as an insurance agent for an registered insurer. Any individual acting as an insurance agent without holding a license is punishable with fine extending to Rs. 50<sup>3</sup> and any insurer or any one acting on behalf of such insurer who appoints as an insurance agent any individual not so licensed, or transacts any insurance business through any such individual, is punishable with fine extending to Rs. 100<sup>4</sup>. The disqualifications referred to above are as follows :<sup>5</sup>

- (a) that the person is a minor;
- (b) that he is found to be of unsound mind by a competent Court;
- (c) that he has been found by a competent court guilty of criminal misappropriation or criminal breach of trust or cheating;
- (d) that in the course of any judicial proceeding relating to any policy or the winding up of an insurance company or in the course of investigation of the affairs of an insurer it has been found that he is guilty of or has knowingly participated in or connived at any fraud, dishonesty or misrepresentation against an insurer or an assured.

A license issued under the Act expires on 31st March every

<sup>1</sup> Insurance Act, 1938. S. 39 (1), (2), (3), (4), (5) & (6).

<sup>2</sup> Ibid. S. 42 (1).

<sup>3</sup> Ibid. S. 42 (2).

<sup>4</sup> Ibid. S. 43 (2).

<sup>5</sup> Ibid. S. 42 (4).

year and must be renewed from year to year on payment of a fee of Re. 1/- unless the holder is in the meantime disqualified<sup>1</sup>. If after the grant of a license it is found that the holder suffers from any of the disqualifications mentioned above the Superintendent of Insurance must cancel the license. Where an agent knowingly contravenes any provision of the Act the Superintendent may cancel his license.

### **Register of Insurance Agents :**

Every insurer and every person who acting on behalf of an insurer employs licensed insurance agents shall maintain a register showing the name and address of every licensed insurance agent appointed by him and the date on which his appointment began and the date, if any, on which his appointment ceased<sup>2</sup>.

### **Commission :**

No person can pay or contract to pay, after six months from the commencement of the Act, any remuneration or reward whether by way of commission or otherwise for soliciting or procuring insurance business in India to any person who is not a licensed agent<sup>3</sup>. The remuneration for licensed agents has been laid down as follows<sup>4</sup> :—

- (a) no insurer can pay or contract to pay any licensed agent as commission or remuneration in amount exceeding, in the case of life Insurance business, forty per cent of the first year's premium payable on any policy or policies effected through him and five per cent of a renewal premium, or, in the case of business of any other class, fifteen per cent of the premium
- (b) But insurers, in respect of life insurance business only, may pay, during the first ten years of their business to their insurance agents fifty five per cent of the first year's premium payable on any policy or policies effected through them and six per cent of the renewal premiums.
- (c) No insurer can forfeit or stop payment of renewal

<sup>1</sup> Insurance Act, 1938 S 42 (1)

<sup>2</sup> Ibid, S 42 (5)

<sup>3</sup> Ibid, S 43 (1)

<sup>4</sup> Ibid, S 40 (1)

<sup>5</sup> Ibid, S 40 (2)

commission due to an agent whose employment may have terminated under any agreement by reason only of such termination provided the agent has served him continually and exclusively for ten years and does not

### **Rebates :**

No person is permitted to allow or offer to allow to any other person, as any inducement to effect or renew a policy, any rebate of the whole or part of the commission payable or any rebate of the premium shown in the policy except such rebate as may be allowed in accordance with the published prospectuses or tables of the insurer, nor is any person taking out or renewing a policy allowed to accept such a rebate. A person offering or allowing such rebate is punishable with fine which may extend to Rs. 100/- and any person accepting such an offer or rebate is punishable with fine which may extend to Rs. 50/-.

### **Special Provisions for Policy-holders :**

#### **Avoidance of the Policy :**

An insurer cannot question or avoid a policy, if effected prior to the commencement of the Act, after the expiry of two years from such commencement and, if effected after the commencement of the Act, after the expiry of two years from the date on which it was effected, on the ground of any inaccurate or false statement made in the proposal, or in any report of a medical officer or referee or friend of the insured, or in any other document leading to the issue of the policy unless the insurer can show that such statement was on a material matter and deliberately and fraudulently made by policy-holder knowing it to be false.<sup>1</sup>

#### **Application of British Indian Law :**

The holder of a policy issued by a non-Indian insurer in respect of business transacted in British India has, after the commencement of the act, the right to receive payment of the money secured by the policy in British India, notwithstanding any agree-

<sup>1</sup> Insurance Act, 1938, S. 44.

<sup>2</sup> Ibid. S. 41 (1) & (2).

<sup>3</sup> Ibid. S. 45.

ment to the contrary, and to sue for relief in respect of the policy in any competent Court in British India and in any such suit the law of British India would be applicable<sup>1</sup>

#### **Payment of money into court :**

Where due to conflicting claims in respect of a policy which has matured for payment of insufficiency of proof of title to the amount secured thereby or for any other reason the insurer is unable to ascertain who amongst the claimants has the real title and can give a valid discharge to the insurer, the insurer must, before the expiry of nine months from the date of the maturity of the policy and in the case of death of the insured after six months from such death apply to the court, within whose jurisdiction the place at which the payment is to be made is situate, to pay the money into court. The application for permission to pay into court must be made by a petition verified by an affidavit signed by a principal officer of the insurer setting forth the following particulars, namely —

- (a) the name of the insured person and his address
- (b) if the insured is deceased, the date and place of his death,
- (c) the nature of the policy and the amount secured by it,
- (d) the name and address of each claimant so far as is known to the insurer with details of every notice of claim received,
- (e) the address at which the insurer may be served with notice of any proceeding relating to disposal of the amount paid into court

If on such application it appears to the Court that a satisfactory discharge for the payment of the amount cannot otherwise be obtained by the insurer it must allow the money to be paid into Court and invest the amount in Government securities pending its disposal. On the money being paid the Court will give notice of the same to every ascertained claimant. If any claimant applies to withdraw the money the Court must cause notice of the same to be given to every other ascertained claimant at the cost of the claimant so applying and on such notice being

<sup>1</sup> Insurance Act, 1938, S 46

given the Court adjudicates on the rival claims and disposes of the amount accordingly<sup>1</sup>.

#### **Directions of Insurance Companies :**

Where the insurer is a company incorporated under the Indian companies Act, 1913, and carries on the business of life insurance, not less than one fourth of the whole number of the directors of the company must be elected by the holders of policies of life insurance from amongst holders of policies of life insurance having the qualifications prescribed by the articles of the company<sup>2</sup>.

#### **Restrictions on Dividends and Bonuses :**

No insurer constituted, incorporated or domiciled in British India carrying on the business of life insurance shall in respect of such life insurance business declare or pay any dividend to shareholders or any bonus to policy-holders except out of a surplus ascertained as the result of an actuarial valuation of the assets and liabilities of the insurer<sup>3</sup>.

#### **Prohibition of business on dividing principle :**

No insurer shall after the commencement of the Act begin or in the case of existing companies continue to carry on after three years from that date, any business upon the dividing principle, that is to say, on the principle that the sum secured by the policy is not fixed but depends either wholly or partly on the results of a distribution of certain sums amongst policies becoming claims within certain time-limits. This, of course, does not prevent an insurer from declaring and paying variable amounts as bonuses in addition to the sum secured by the policy based on a periodical actuarial valuation. During the three years after the commencement of the Act when an existing insurer may continue business on dividing principle the insurer must withhold from distribution a sum not less than forty per cent of the premiums received during each year after the commencement of the Act and invest the same so as to make up the amount required for investment under the Act<sup>4</sup>.

<sup>1</sup> Insurance Act, 1937, S. 47.

<sup>2</sup> Ibid, S. 48.

<sup>3</sup> Ibid, S. 49.

<sup>4</sup> Insurance Act, 1938, S. 52.

### **Notice of Options :**

When a policy lapses the insurer must, within three months of the lapsing, give notice to the policy holder informing him of the options available to him<sup>1</sup>

### **Supply of Copies of Proposals and Medical Reports :**

Every insurer must on application by a policy holder and on payment of a fee not exceeding one rupee, supply to the policy-holder certified copies of the questions put to him and his answers thereto contained in his proposal for insurance and in the medical report supplied in connection therewith

### **Surrender Value :**

This subject has already been dealt with

### **Special Provisions relating to external companies :**

If a special requirement is to keep, or deposits or assets is imposed on Indian Companies by my country as a condition of carrying on insurance business in that country Reciprocal and no such requirement is imposed on insurers constituted incorporated or domiciled in such other country under the Act then the Central Government if satisfied of the existence of such discrimination in requirements on Indian Companies in such other country by notification in the Official Gazette direct the same or similar requirements to be imposed upon insurers of such other country as a condition of carrying on the business of insurance in British India

Every insurer having his principal place of business or domicile outside British India, who establishes a place of business within British India or appoints a representative in British India with the object of obtaining insurance business, must, within three months from the establishment of such place of business or the appointment of such agent, file with the Superintendent of Insurance, the following particulars :—

(a) a certified copy of the Charter, statutes, deeds of settle-

<sup>1</sup> Ibid, S 50

<sup>2</sup> Ibid, S 51

<sup>3</sup> Ibid, S 62

ment, or memorandum and articles or other instrument constituting or defining the constitution of the insurer, and, if the instrument is not in the English language a certified translation thereof;

- (b) a list of the directors, if the insurer is a company,
- (c) the name and address of some one or more persons resident in British India authorised to accept on behalf of the insurer service of process and any notice required to be served on the insurer, together with a copy of the power of attorney granted to him,
- (d) the full address of the principal office of the insurer in British India
- (e) a statement of the classes of a marine business to be carried on by the insurer and
- (f) a statement verified by an affidavit setting forth the special requirements, if any, to which Indian Companies are subject as a condition of carrying on insurance business in his country.

If there is any alteration in any of the above particulars at any time the insurer must furnish to the Superintendent of Insurance particulars of such alteration forthwith.

Every insurer having his principal office of business or domicile outside British India must keep at his principal office in British India such books of account registers and documents as will enable the receiver's statements, and abstracts which he is required under the Act to furnish to the Superintendent of Insurance in respect of the insurance business transacted by him in India to be completed and, if necessary, checked by the Superintendent.

#### **Winding up :**

The Court may order the winding up of an insurance company on all the grounds set out in ss 161 and 163 of the Indian Companies Act. In addition to these grounds the Court may order the winding up of an insurance company under the Act on the following grounds<sup>1</sup> —

- (a) If with the sanction of the Court previously obtained a petition is presented by not less than one tenth of

<sup>1</sup> Insurance Act, 1938, S 53.

all the shareholders holding not less than one tenth of the whole share capital or by not less than fifty policy-holders holding policies which have been in force for not less than three years and are of the total value of not less than Rs 50,000/-, or

- (b) If the Superintendent of Insurance, who is authorised to do so, applies in this behalf to the Court on any of the following grounds, namely—
  - (i) that the company has failed to deposit or to keep deposited with the Reserve Bank the amounts required by S 7, or S 98 of the Insurance Act ,
  - (ii) that the company has failed to comply with any requirement of the Insurance Act and has continued such failure for a period of three months after notice of such failure has been conveyed to the company by the Superintendent of Insurance ,
  - (iii) that it appears from the returns furnished under the provisions of the Act or from the results of any investigation made thereunder that the company is insolvent , or
  - (iv) that the continuance of the company is prejudicial to the interests of the policy holders

An insurance company cannot be wound up voluntarily except for the purpose of effecting an amalgamation or a reconstruction of the company or on the ground that by reason of its liabilities it cannot continue its business<sup>1</sup>

#### **Winding up of Secondary Companies :**

When the insurance business or any part thereof of an insurance company is transferred to another insurance company under any arrangement the transferor company is known as the "Secondary Company" and the transferee company is known as the "principal company". If the principal company is being wound up by or under the supervision of the Court, the Court must also order the secondary company to be wound up in conjunction with the principal company and may appoint the same person to be the liquidator for the two companies and may make provision for such other matters as may be necessary in view of the companies

<sup>1</sup> The Insurance Act, 1938, S 54

being wound up as if they were one company. An application may also be made in relation to the winding up of the secondary company in conjunction with the principal company by any creditor of, or person interested in, the principal or the secondary company. Unless otherwise ordered the winding up of the secondary company will commence at the same time as that of the principal company. Before ordering the winding up of the secondary company the Court must hear all objections relating thereto where the winding up of the secondary company does not commence at the same time as that of the principal company.<sup>1</sup>

In adjusting the rights and liabilities of the members of principal and secondary companies among themselves the Court must have regard to the constitution of the

**Adjustment of rights and liabilities between principal and secondary companies.**

companies, in pursuance of which the transfer had taken place, in the same manner as the Court has regard to the rights and liabilities of different classes of contributors in the case of the winding up of a single company or as near thereto as

possible. Where a company stands in the relation of a principal company to one insurance company and in the relation of a secondary company to some other insurance company or where there are several insurance companies standing in the relation of secondary companies to one principal company, the Court may deal with any number of such companies together or in separate groups as it thinks most expedient upon the principles stated above."

#### **Valuation of Liabilities :**

In the winding of an insurance company or in the insolvency of any other insurer, the value of the assets and the liabilities of the insurer must be ascertained in such manner as the liquidator or receiver in insolvency thinks fit subject to any directions which the Court may give and in the case of current contracts in respect of life insurance business, according to the method and basis, to be determined by an actuary approved by the Court.<sup>2</sup>

#### **Application of Surplus Assets of Life Insurance Fund :**

In the winding up of an insurance company and in the

<sup>1</sup> Insurance Act, 1938, S. 57 (1), (2), (4) & (5).

<sup>2</sup> Ibid, S. 57 (3) & (6).

<sup>3</sup> Insurance Act, 1938, S. 55 (1).

insolvency of any other insurer the value of the assets and liabilities of the insurer in respect of life insurance business must be ascertained separately from the value of any other assets or any other liabilities of the insurer and no such assets can be applied to the discharge of any liabilities other than those in respect of life insurance business except when there is a surplus of assets over liabilities in respect of life insurance business. In ascertaining the amount of surplus, in case there is such a surplus, addition to liabilities is to be made where any portion of the profits on the whole business had been allocated by the insurer to policy-holders in respect of life insurance business. The addition is to be of an amount which is of the same proportion of the surplus without such addition as the profits allocated bear to the profits allocated to the policy-holders during the ten years immediately preceding the winding up or insolvency. The following example will make it clear —In winding up the assets of company 'A' in respect of life insurance business exceed liabilities by Rs. 10,000/- Rs. 20,000/- being assets and Rs. 10,000 - being liabilities. But before the winding up, company 'A' allocated Rs 1000/- being portion of the profits to life policy holders. During ten years preceding the winding up Rs 10,000/- was allocated to life-policy holders out of the profits. Therefore the surplus of assets in respect of life insurance business will not be Rs. 10,000 but  $(Rs\ 20,000) / (Rs\ 10,000 + 1000)$  =Rs. 9000. The sum of Rs 1000, which is added to liabilities is  $\frac{1}{10}$  of Rs 10,000 - (being the surplus without such addition) which is of the same proportion as the sum allocated for profits i.e., Rs 1000 - bears to the total sum of profits allocated during the preceding ten years i.e., Rs 10,000. But the Court may vary the proportion of the sum to be added if it thinks that the above formula is inequitable in the circumstances or that there has been no allocation of profits.<sup>1</sup>

#### Reduction of Contracts of Insurance :

In the case of liquidation of an insurance company or the insolvency of an insurer the Court may reduce the amount of insurance contracts of all classes of the company or the insurer upon such terms and subject to such conditions as the Court thinks

<sup>1</sup> Insurance Act, 1936, S 56 (1) & (2)

just. But where, prior to winding up, a company carrying on the business of life insurance has been proved to be insolvent, the Court may, if it thinks fit, reduce the amount of insurance contracts upon such terms and subject to such conditions as the Court thinks fit instead of making a winding up order. Orders as above can be made only on an application to be made either by the liquidator or by or on behalf of the company, or by a policy-holder or by the Superintendent of Insurance.<sup>1</sup> For the purpose of any such reduction of contracts the value of the assets and liabilities of the company and all claims in respect of policies issued by it must be ascertained according to the directions of the Court if any and subject to the rule that the liabilities on all current contracts effected in the course of life insurance business including annuity business is to be calculated by the method and upon the basis to be determined by an actuary approved by the Court.<sup>2</sup>

#### **Partial winding up :**

If at any time it appears expedient that the affairs of an insurance company (not any other insurer) in respect of any class of business comprised in the undertaking of the company should be wound up but that any other class of business comprised in the undertaking should continue to be carried on by the company or be transferred to another insurer, a scheme for such purpose may be prepared and submitted to the Court and, on its being sanctioned by the court, it will become effective. But any such scheme must provide for the allocation and distribution of the assets and liabilities of the company between any classes of business affected (including the allocation of any surplus assets which may arise in relation to the part of the business wound up) and also for the future rights of the different classes of policy-holders and the manner for winding up the part of the business proposed to be wound up. In calculating the assets and liabilities and the allocation thereof for this purpose the same rules as to valuation as referred to above should be adhered to.<sup>3</sup>

<sup>1</sup> Ibid, S. 61 (1), (2) & (3).

<sup>2</sup> Ibid, S. 55 (2) & 6th Schedule.

<sup>3</sup> Insurance Act, 1938, S. 58.

### **Provident Societies :**

#### **Definition :-**

Provident society means a person, or partnership or a company which receives premiums or contributions for securing annuities on human life not exceeding Rs 50/- or for a fixed sum, not exceeding Rs 500/- exclusive of any profits or bonus, to be paid on the happening of any of the following contingencies<sup>1</sup> —

- (a) the birth, marriage or death of any person or the survival by a person of a stated age or contingency
- (b) failure of issue
- (c) the occurrence of a social, religious or other ceremonial occasion
- (d) disablement in consequence of sickness or accident
- (e) the necessity of providing for the education of a dependent and
- (f) any other contingency which may be prescribed or authorised by the Provincial Government with the approval of the Central Government

#### **Name :**

A provident society if started after the commencement of the Act must adopt and, if started before such commencement, must continue to use after six months of such commencement as its name words which include the word provident and exclude the word life.

#### **Insurable Interest :**

No provident society can issue a policy whereby the money accrued by it is payable to any person other than the person paying the premium thereon or the wife, husband, child, grand child, parent, brother or sister, nephew or niece of such person. In other words a person is deemed to have an insurable interest in the lives of these relations only for the purpose of provident insurance<sup>2</sup>.

#### **Dividing Business :**

No provident society like an insurer can carry on business on

<sup>1</sup> Ibid, Ss 65 & 66

<sup>2</sup> Insurance Act, 1938, S 67

<sup>3</sup> Insurance Act, 1938, S 58.

the dividing principle<sup>1</sup>. But where a society had been doing business on the dividing principle at the commencement of the Act, the Superintendent may allow the society to continue the old business on dividing principle for a period not exceeding two years with a view to reorganising its business on new lines prescribed by the Act provided the society applies within three months from the commencement of the Act for permission to do so and does not enter into any new business on the dividing principle after the commencement of the Act. If a society carries on business on the dividing principle excepting as aforesaid the Superintendent of Insurance is under a duty to take steps, as soon as possible, to have the society wound up.<sup>2</sup>

### **Registration :**

No provident society except one registered under the Provident Insurance Societies Act, 1912, can receive any premium or contribution until it has obtained from the Superintendent of Insurance a certificate of registration.<sup>3</sup> Every application for registration must be accompanied by the following :<sup>4</sup>

- (a) A certified copy of the Memorandum and Articles of Association in case the society is a company or a certified copy of the deed of constitution of the society in case it is not a company and in every case a certified copy of the rules of the society :
- (b) the names and addresses of the proprietor, or directors, and the managers of the society ;
- (c) certificate from the Reserve Bank of India that the deposit required under the Act as mentioned below has been made ; and
- (d) a declaration verified by an affidavit that the minimum working capital required under the Act is available.

If the superintendent is satisfied that all the requirements of the Act have been complied with, he will register the society and its rules and issue a certificate of registration and he may refuse to issue such a certificate until he is so satisfied.<sup>5</sup>

<sup>1</sup> See ante for the meaning of dividing principle.

<sup>2</sup> Ibid, S. 69.

<sup>3</sup> Ibid, S. 70 (1).

<sup>4</sup> Ibid, S. 90 (2).

<sup>5</sup> Insurance Act, 1938. S. 70 (3).

### Cancellation of Registration :

The Superintendent of Insurance may cancel the registration of a society if he obtains the sanction of the Court to do so after giving previous notice in writing to the society specifying the grounds for the proposed cancellation and allowing the society an opportunity of being heard. The grounds on which the Superintendent may apply for and effect cancellation of registration of a society are the following<sup>1</sup> —

- (a) If he is satisfied as the result of an enquiry made by him under s. 87 of the Act—
  - (i) that the society is insolvent or is likely to become so or
  - (ii) that the business of the society is conducted fraudulently or not in accordance with the rules thereof, or that it is in the interests of the policy holders that the society should cease to carry on business
- (b) If the deposit required under the Act have not been made or
- (c) If the society, having failed to comply with any requirements of the Act has continued such failure for a period of one month after notice of such failure has been conveyed to the society by the Superintendent of Insurance.

But where the society is insolvent or likely to become so as under clause (a) (i) above the Superintendent may, instead of applying for cancellation of registration, make a recommendation to the court that the contracts of the society should be reduced in such manner and subject to such conditions as he may indicate.

### Working Capital :

Every provident society established after the commencement of the Act, must have a paid up capital sufficient to provide as working capital a net sum of not less than Rs. 5000/- exclusive of deposits made under the Act and in the case of a company exclusive of any expenses incurred in connection with the formation of the company. Otherwise the society will not be registered.<sup>2</sup>

<sup>1</sup> Ibid S 70 (4)

<sup>2</sup> Insurance Act 1938 S 72

### **Deposits :**

Every provident society must, if established before the commencement of the Act within one year from such commencement, or, if established after the commencement of the Act before the society applies for registration, deposit and keep deposited with one of the offices of the Reserve Bank of India, for and on behalf of the Central Government, cash or approved securities amounting at the market value of the securities on the date of the deposit to Rs. 5000/- and must thereafter make each year a further deposit amounting to not less than one fifth of the gross premium income for the year until the total amount so deposited and kept come upto Rs. 50,000/-.<sup>1</sup>

### **Rules :—**

Every provident society established after the commencement of the Act must set forth in its rules the following:—

- (a) the name, the object and the location of the registered office of the society;
- (b) the contingencies or the classes of contingency on the happening of which money is to be paid;
- (c) the conditions to be complied with before, and the payments to be made on, admission to the society;
- (d) the rates of premium or contribution, and the periods for which or the times at which premiums or contributions are payable;
- (e) the maximum amount payable to a subscriber or policy-holder;
- (f) the nature and amounts of the benefits provided for by the society;
- (g) the circumstances in which any bonus may be paid to a policy-holder;
- (h) the nature of the evidence required for the proof of the happening of any contingency on which money is to be paid;
- (i) the circumstances in which policies may be forfeited or renewed or the whole or a part of the premiums paid on

<sup>1</sup> Ibid, S. 73.

<sup>2</sup> Ibid, S. 74 (1).

- a policy may be renewed, or a surrender value of a policy may be granted;
- (j) the penalties for delay in paying or failure to pay premiums or contributions;
  - (k) the proportion of the annual income of the society which may be disbursed on and the provisions to be made for meeting the expenses of the management of the society;
  - (l) the person or persons who or the authority which shall have power to invest the funds of the society;
  - (m) the provisions for appointment of auditors and their remuneration;
  - (n) the procedure to be adopted in altering the rules of the society;
  - (o) the following unless these are provided for in the articles of association of a society which is a company incorporated under the Indian Companies Act, 1913,—
  - (r) the mode of appointment and removal, the qualification and the powers of a director manager, secretary or other officer of the society,
  - (s) the manner of raising additional capital;
  - (m) the provisions for the holding of general meetings of the members and policy holders and for the powers to be exercised and the procedure to be followed thereat and
  - (p) Such other matters as may be prescribed.

Where the rules of any provident society registered under the Provident Insurance Societies Act, 1912, do not contain the particulars mentioned above, the society must, before the expiry of one year from the commencement of the Act, amend the rules so as to comply with the above requirements.

#### **Amendment of Rules :**

No amendment of any rule of a provident society is valid until it has been sent to and duly registered by the Superintendent of Insurance. The Superintendent will register the amendment if he is satisfied that the proposed amendment is neither contrary to the provisions of the Act nor does it unfairly affect the rights of existing members or policy-holders of the society.<sup>1</sup>

<sup>1</sup> Insurance Act, 1938, S 75.

### **Register of Books :**

Every provident society must keep at its registered office<sup>1</sup>—

- (a) a register of members in which will be entered the name, address and occupation, if any, of every proprietor, director, manager or secretary and of every member of the society ;
- (b) a register or record of policies in which must be entered, in respect of every policy issued by the society, the name and address of the policy holder, the date when the policy was effected and a record of any transfer, assignment or nomination of which the society has notice ;
- (c) a register of claims in which must be entered every claim made, together with the date of the claim, the name and address of the claimant and the date on which the claim is discharged or in the case of a claim which is rejected the date of rejection and the grounds therefor ;
- (d) a register of agents in which shall be entered the name and address of every agent employed by the society ;
- (e) a cash book in which must be entered separately for each class of contingency mentioned above all sums received and expended by the society and the matters in respect of which the receipt or expenditure takes place ;
- (f) a ledger ; and
- (g) a journal.

### **Revenue Account and Balance-sheet :**

Every provident society must at the expiry of each calendar year prepare a revenue account and balance sheet in the prescribed manner, together with a report on the general state of the society's affairs and have the revenue account and the balance sheet audited by an auditor who shall have all the powers given to an auditor under s. 145 of the Indian Companies Act.<sup>2</sup>

### **Annual Statements :**

Every provident society must at the expiry of each calendar year prepare with respect to that year

<sup>1</sup>Ibid, S 79

<sup>2</sup>Insurance Act, 1939, S 80 (1)

<sup>3</sup>Ibid, S 80 (2).

- (a) a statement showing separately for each class of total amount insured thereby and the total premium income received in respect thereof and the number of existing policies discontinued during the year with the total amount insured thereby, and  
 (i) the total amount of claims made and the total amount paid in satisfaction thereof;
- (b) a statement showing details of every insurance effected on a life other than the life of the person insuring e.g., details regarding B when A effects a policy on the life of B.
- (c) a statement showing the total amount paid as allowances to agents and canvassers.

#### **Actuarial Report and Abstract :**

Every provident society must once in every five years or at such shorter intervals as may be laid down by the rules of the society cause an investigation to be made into its financial condition including the valuation of its liabilities and assets by an actuary.<sup>1</sup> The report of the actuary must contain an abstract which is to specify<sup>2</sup>—

- (a) the general principles adopted in the valuation, including the method by which the valuation age of lives was ascertained;
- (b) the rate at each age of the mortality and any other factor assumed and the annuity values used in valuation;
- (c) the reserve values held against policies effected;
- (d) the rate of interest assumed, and
- (e) the provision made for expenses.

A certificate by a principal officer of the society, that all materials necessary for proper valuation have been placed at the disposal of the actuary and that full and accurate particulars of every policy under which there is a liability, actual or contingent, have been furnished to the actuary for the purpose of investigation, must be appended to the report of the actuary.

If the actuary finds that the financial condition of the society is such that no surplus exists for distribution as bonus to the policy-

<sup>1</sup> Insurance Act, 1938, S. 81 (1).

<sup>2</sup> Ibid, S. 81 (2).

holders or as dividend to the share-holders he is to state in his report whether in his opinion the society is insolvent and, if so, whether it shall be wound up or not, and the extent to which in his opinion existing contracts should be modified or existing rates of premium should be adjusted to make good the deficiency in the assets<sup>1</sup>

#### **Submission of Returns and Abstracts :**

The revenue account and balance sheet with the auditor's report thereon, report of the general state of the society's affairs, annual statements, actuarial abstracts referred to above must be furnished by a society as returns to the Superintendent of Insurance within three months from the end of the period to which they relate -

#### **Supply of Documents :**

Every provident society must on demand deliver free of cost to any member of the society and to any non member at a charge not exceeding Re 1/- 1 copy of the rules of the society<sup>2</sup>. Every provident society must send to any member or policy-holder copies of the revenue account, the auditor's report, and report on the general state of the society's affairs within fourteen days from the receipt of the application made in this behalf and on payment of a fee not exceeding Re 1/- provided the application is made within two years from the date on which the document or documents were furnished to the Superintendent<sup>3</sup>.

#### **Actuarial Examination of Schemes :**

In the case of a society established after the commencement of the Act, every scheme of insurance which it proposes to put into operation must be examined by an actuary and the society cannot receive any premium or contribution in connection with the scheme until the actuary has certified that the scheme is sound and such certificate has been forwarded to the Superintendent of Insurance

In the case of a society registered before the commencement of the Act, the requirement is the same as regards new schemes

<sup>1</sup> Insurance Act, 1938, S. 81 (3).

<sup>2</sup> Ibid, S. 82 (1)

<sup>3</sup> Ibid, S. 76

<sup>4</sup> Ibid, S. 82.

which it proposes to put into operation after the commencement of the Act. In regard to old schemes, the society must submit all schemes of insurance which the society has in operation at the commencement of the Act to examination by an actuary and send the report of the actuary thereon to the Superintendent of Insurance before the expiry of six months from the commencement of the Act. The report of the actuary must state in respect of each scheme whether it is actuarially sound, and where no actuarial report has been made within two years preceding the report, the report must also state whether the assets of the society are sufficient to meet its liabilities under the existing schemes, and if not, how in the opinion of the actuary the existing contracts should be modified. If any scheme is reported by the actuary to be actuarially unsound, the Superintendent of Insurance must give notice to the society prohibiting the operation of the scheme; and the society cannot receive any premium or effect any policy in connection with the scheme after the expiry of one month from the receipt of the notice. Where a scheme is thus discontinued, the society must set apart out of its assets the sum sufficient in the opinion of the actuary to meet the liabilities incurred under the scheme so discontinued when its assets are sufficient to meet all existing liabilities. But if its assets are not sufficient to meet all existing liabilities it must apply to the Court within three months from such discontinuance for a modification of its existing contracts or failing such modification for the winding up of the society.<sup>1</sup>

#### **Separation of Accounts and Funds :**

Where a provident society effects policies of insurance in connection with more than one of the classes of contingency mentioned above, the receipts and payments in respect of each such class must be recorded in a separate account in the cash book which is to be kept accordingly.<sup>2</sup>

#### **Investment and Loan :**

Every provident society must invest all surplus assets in Government securities or securities mentioned in s. 20 of the

<sup>1</sup> Insurance Act, 1938, S. 84.

<sup>2</sup> Ibid, S. 85.

Indian Trusts Act until the total amount invested amounts to not less than fifty per cent of the total assets of the society and keep the same invested to the extent of such fifty per cent unless it already holds invested in such securities not less than fifty per cent of its total assets.<sup>1</sup> The funds or investments of a provident society except the deposit kept with the Reserve Bank must be kept in the name of the society.

No provident society can advance any loan to any of its directors or officers out of its assets except on the security of a policy of insurance held in the society and to the extent of the surrender value of such policy or to any concern of which a director or officer of the society is a director or partner.<sup>2</sup>

Any director or officer of a society, which advances a loan in contravention of the above provision, who is knowingly a party to the above contravention will be jointly and severally liable to the society for the amount of the loan and such amount together with interest not exceeding 12% per annum will be recoverable by execution on the application by the Superintendent of Insurance to any competent Court as if a decree for such amount had been passed by that Court. Such director or officer is also liable for other penalties provided by the Act.<sup>3</sup>

#### **Inspection of Books :**

The books of every provident society must at all reasonable times be open to inspection by the Superintendent of Insurance or any person appointed by him for the purpose or by any member or policy-holder of the society who has made an application for the purpose to the Superintendent of Insurance.<sup>4</sup>

#### **Inquiry by the Superintendent of Insurance :**

The Superintendent of Insurance must at least once in two years and may, at any other time, if he thinks fit, visit personally or depute a suitable person to visit the principal office of a provident society and inquire into the solvency of the society and the manner

<sup>1</sup> Ibid, S. 85 (3).

<sup>2</sup> Ibid, S. 85 (4).

<sup>3</sup> Ibid, S. 85 (4).

<sup>4</sup> Ibid, S. 86.

in which the business of the society is conducted, or may, after giving notice to the society and giving it an opportunity to be heard, direct such an enquiry to be made by an auditor or actuary appointed by him.<sup>1</sup> For the purpose of any such enquiry the superintendent or the auditor or actuary, as the case may, will be entitled to examine all books and documents of the society and may demand from the society or any officer of the society such explanations as he may require on any matter relating to the affairs of the society.<sup>2</sup> The results of any such enquiry are to be recorded in a report which is to be kept in the office of the Superintendent and a copy of the Report must be sent to the society concerned and be open to inspection by any member or policy-holder of the society.<sup>3</sup>

#### **Managing Agents :**

A provident society, like an ordinary insurance company, cannot employ a managing agent and the prohibition is the same as in the case of ordinary insurance companies.

#### **Assignment and Nomination :**

The assignment and nomination of a policy in a provident society is subject to the same law as in the case of assignment of a life insurance policy. We have already studied it. The only difference in the case of a policy in a provident society is that in regard to nomination, no nomination is valid unless the nominee is the husband, or wife, or father, or mother, or child, or grandchild, or brother, or sister, or nephew, or niece of the holder of the policy.<sup>4</sup>

#### **Reduction of Insurance Contracts :**

The Court may make an order reducing the amount of the insurance contracts of a provident society upon such terms and subject to such conditions as the Court thinks just on the following grounds<sup>5</sup>—

- (a) If where the society is insolvent or is likely to become

<sup>1</sup> Ibid. S. 87 (1).

<sup>2</sup> Ibid. S. 87 (2).

<sup>3</sup> Ibid. S. 87 (3).

<sup>4</sup> Insurance Act, 1938, S. 97 (2).

<sup>5</sup> Ibid. S. 89.

so, the Superintendent applies to the Court recommending that the contracts of the society should be reduced in such manner and on such conditions as he may indicate as an alternative to cancelling the registration of the society :

- (b) If while a society is in liquidation the Court thinks fit.
- (c) If when a society has been proved to be insolvent the Court thinks fit to do so in place of making an order for the winding up of the society : or
- (d) If the Court is satisfied on an application made in this behalf by the society supported by the report of an actuary, and after giving the policy-holders an opportunity to be heard that it is desirable to do so.

#### **Winding up :**

In addition to the grounds on which a company may be wound up by Court under the Indian Companies Act, 1913, the Court may order the winding up of a society if its registration is cancelled and in such a case the Superintendent may himself order the winding up of the society.<sup>1</sup> But a provident society cannot be wound up voluntarily whether it is a company or not except for the purpose of effecting an amalgamation or reconstruction of the society or on the ground that by reason of its liabilities it cannot continue its business.

#### **Appointment of Liquidator :**

When a provident society is wound up either by Court or voluntarily, the society must give notice of the order or resolution authorising the winding up to the Superintendent of Insurance within seven days from the date of such order or resolution. In a voluntary liquidation the Superintendent must appoint the liquidator and fix his remunerations. Such a liquidator may be removed by the Superintendent if he fails to discharge his duties properly.<sup>2</sup>

#### **Powers of Liquidator :**

A liquidator appointed to wind up a society has the power<sup>3</sup> :—

<sup>1</sup> Ibid, S. 88.

<sup>2</sup> Insurance Act, 1938, S. 90.

<sup>3</sup> Ibid, S. 91.

- (a) to institute or defend any legal proceedings on behalf of the society by his name of office ;
- (b) to determine the contribution to be made by members of the society respectively to the assets of the society ; the liquidator has the same power for settling the list of contributories and realising the amount of contribution, as of the official liquidator under the Indian Companies Act, 1913.
- (c) to investigate all claims against the society and to decide questions of priority arising between claimants ;
- (d) to determine by what persons and in what proportion the costs of the liquidation are to be borne ;
- (e) to give such directions in regard to the collection and distribution of the assets of the society as may appear to him to be necessary for winding up the affairs of the society.
- (f) to summon, and enforce the attendance of, witnesses and to compel the production of documents by the same means and as far as may be in the same manner as is provided in the case of civil courts ; and
- (g) with the sanction of the Superintendent of Insurance, to employ such establishment and to obtain such assistance from an actuary or an auditor as may be necessary for the discharge of his duties.

#### **Procedure at Liquidation :**

*Collecting the property*—The liquidator must take charge of all property moveable or immoveable of the society and of all its books and documents.<sup>1</sup> If any proprietor or officer of the society fails to deliver to the liquidator any book or document when so required by the liquidator, he will be punishable with imprisonment which may extend to six months, or with fine which may extend to Rs. 500/- or both and the Court may order the delivery of the assets or book or document to the liquidator.<sup>2</sup>

#### **Creditors' Meeting :**

The liquidator must hold a meeting of creditors between twenty one and twentyeight days after his appointment and he

<sup>1</sup> Insurance Act, 1938, S. 92 (1).

<sup>2</sup> Ibid, S. 92 (2).

must send notice by post of such meeting within fifteen days of his appointment to every person who appears to him to be a creditor of the society specifying the date, hour and place of the meeting and also advertise notice of the meeting once in the local official Gazette and once at least in two newspapers circulating in the province in which the society is situated.<sup>1</sup>

*Committee of Inspection* :--At the meeting of the creditors so convened the creditors are to determine whether they should apply for the appointment of any person as liquidator in the place of or jointly with the liquidator already appointed, or for the appointment of a committee of inspection. If they decide on any one of the above courses open to them they must apply by a creditor chosen for the purpose to the Superintendent of Insurance within fourteen days after the date of the meeting conveying their decision and the Superintendent is to appoint thereupon a suitable person in place of or jointly with the liquidator already appointed or, if so desired, a committee of inspection.<sup>2</sup> If a committee of inspection is appointed, it will, subject to any prescribed conditions, have a general power of supervision over the acts of the liquidator and will have the right to inspect his account at all reasonable times.<sup>3</sup>

#### **Ascertainment of Liabilities and Assets :**

The liquidator is to ascertain as soon as possible, with such assistance from an actuary as may be required, the amount of the society's liability to every person appearing by the society's books to be entitled to or interested in any policy issued by the society and is to give notice of the amount so found to each such person in the prescribed manner and each such person on receiving such notice will be bound by the value so ascertained.<sup>4</sup>

The liquidator must also make a valuation of the assets of the society and an estimate of the costs of the winding up and settle the list of contributors on the basis of these.<sup>5</sup>

#### **Collection of Deposit and Distribution of Asset :**

The liquidator must also apply to the Superintendent of

<sup>1</sup> Ibid. S. 91 (3).

<sup>2</sup> Insurance Act, 1938 S. 92.

<sup>3</sup> Ibid. S. 92.

<sup>4</sup> Ibid. S. 92 (6)

<sup>5</sup> Ibid. S. 92

Insurance for the return of the deposit who must order the return of the same on such application subject to such terms and conditions as he may think fit.<sup>1</sup> In administering and distributing the assets of the society the liquidator must have regard to any directions that may be given by the creditors or contributors at a general meeting or by the Superintendent of Insurance.<sup>2</sup>

The liquidator must keep books of account in which he must record the proceedings at all meetings attended by him, all amounts received or expended by him and any other matter that may be prescribed, and these books may, with the sanction of the Superintendent, be inspected by any creditor or contributory.<sup>3</sup>

If the winding up continues for more than a year, the liquidator must summon a meeting of the creditors and contributors at the end of the first year and of each succeeding year, and must lay before them an account of his acts and dealings and of the conduct of the winding up and such account together with any views expressed thereon by the meeting must be forwarded by the liquidator to the Superintendent of Insurance.<sup>4</sup>

Subject to the provisions of the Act the liquidator should as far as practicable follow the procedure prescribed for the official liquidator under the Indian Companies Act, 1913.<sup>5</sup>

#### **Dissolution of Provident Society :**

As soon as the affairs of a provident society are fully wound up the liquidator must prepare an account of the winding up showing how the winding up has been conducted and the property of the society has been disposed of and must call a meeting of members, creditors, and contributors for the purpose of laying before it the account and giving any explanation thereof.<sup>6</sup> Notice of the meeting has to be sent to each person individually and advertised in the local official Gazette and in at least two newspapers circulating in the province in which the society is situated.<sup>7</sup>

Within one week after the meeting the liquidator must send

<sup>1</sup> Ibid, S. 92 (8).

<sup>2</sup> Insurance Act, 1938 S. 92 (d).

<sup>3</sup> Ibid, S. 92 (10).

<sup>4</sup> Ibid, S. 92 (11).

<sup>5</sup> Ibid, S. 92 (12).

<sup>6</sup> Ibid, S. 93 (1).

<sup>7</sup> Ibid, S. 93 (2).

to the Superintendent of Insurance a copy of the account and report to him the holding of the meeting and its date and forward to him a copy of the proceedings of the meeting.<sup>1</sup> The Superintendent may return the account to the liquidator if it is incomplete or unsatisfactory and may require the liquidator to carry out any further steps necessary to complete the winding up and the liquidator must comply with such requirement and submit a further report to the Superintendent within six months.<sup>2</sup> But if the Superintendent is satisfied that the affairs of the society have been fully wound up he must register the account of the liquidator who has to forthwith make over to the Superintendent such sums, if any, as might remain undisposed of. On the expiry of three months from the registering of the account the Superintendent must declare the society dissolved and notify the dissolution in the local official Gazette and the liquidator will thereupon be discharged from further responsibility.<sup>3</sup> The sums, if any, made over by the liquidator, to the Superintendent prior to his discharge become the property of the Government if no order is obtained by any claimant from a competent court in respect of the disposal of such sums within a period of five years from the date on which such sums were made over to the Superintendent.<sup>4</sup>

#### **Mutual Insurance Companies and Co-operative Life Insurance Society :**

##### **Definition :**

A mutual insurance company means an insurer, being a company incorporated under the Indian Companies Act, 1913, which has no share capital and of which by its constitution only all policy-holders are members.<sup>5</sup>

A co-operative life insurance society means an insurer being a society registered under the co-operative societies Act, 1912, or under an act of a Provincial Legislature governing the registration of co-operative societies, which carries on the business of life insurance and which has no share capital on which dividend or bonus is payable and of which by its constitution only original members

<sup>1</sup> Insurance Act, 1938, S. 93 (3).

<sup>2</sup> Ibid, S. 93 (4).

<sup>3</sup> Ibid, S. 93 (5).

<sup>4</sup> Ibid, S. 93 (6).

<sup>5</sup> Insurance Act, 1938, S. 95 (1).

on whose application the society is registered and all policy-holders are members.<sup>1</sup>

Other co-operative societies (*i.e.*, societies not carrying on life insurance business) may be admitted as members of a co-operative life insurance society, without being eligible to any dividend, profit or bonus.<sup>2</sup>

A provincial Government may, subject to any rules made by the Central Government, empower the Registrar of co-operative societies of the province to register co-operative societies for the insurance of cattle or crops or both under the provisions of the co-operative societies Act in force in the province. A provincial Government may also make rules not inconsistent with any rules made by the Central Government to govern such societies and if any provision in the Act is inconsistent with those rules, such provision will not to that extent apply to such societies.

#### **Working Capital :**

The earlier provisions of the Act in respect of working capital do not apply to a mutual insurance company or to a co-operative insurance society.<sup>3</sup> The requirement as to working capital for these are as follows. No mutual insurance company incorporated after 26th January, 1937 and no co-operative insurance society registered after that date can be registered under the Act, unless it has as working capital a sum of Rs. 15,000/-exclusive of deposit to be made before or at the time of applications for registration and of preliminary expenses, if any, incurred in the formation of the company or society.<sup>4</sup>

#### **Deposit :**

Every Mutual Insurance Company and every co-operative life insurance society must, in respect of the life insurance business carried on by it in British India, deposit and keep deposited with one of the offices in India of the Reserve Bank of India, for and on behalf of the Central Government, a sum of Rs. 2,00,000/- in cash or in approved securities estimated at the market value of the

<sup>1</sup> *Ibid.*, S. 95 (1).

<sup>2</sup> *Ibid.*, S. 95 (2).

<sup>3</sup> *Ibid.*, S. 95 (3).

<sup>4</sup> *Ibid.*, S. 96.

<sup>5</sup> Insurance Act, 1938 S. 97.

securities on the day of deposit.<sup>1</sup> The deposit may be made in instalments of which the first instalment must be of Rs. 25,000/- to be made before or at the time of the application for registration and the subsequent instalments must be annual instalments made before the expiry of each subsequent year of an amount in cash or in approved securities estimated at the market value of the securities on the day of the payment of the instalment, equal to one-third of the gross premium income received in the previous year.<sup>2</sup>

#### **Assignment and Transfer :**

The law relating to assignment is the same with regard to policies issued by these companies or societies as in the case of other policies excepting that an assignee or a transferee will not become a member of a mutual insurance company or a co-operative insurance society merely by reason of any such transfer or assignment.<sup>3</sup>

#### **Publication of Notices and Documents :**

Notwithstanding anything contained in the Indian Companies Act, 1913, a mutual Insurance company and a co-operative Life Insurance Society may, instead of sending the notices and the copies of the balance sheet, revenue account, and other documents which they are required to send to the members under the Indian Companies Act, 1913, secs. 79 and 131, publish such notices or documents once in a newspaper published in the English language and in a newspaper published in one Indian language circulating in the place where the principal office of the company is situated and, in case any members of the company are domiciled in any other province, in a newspaper or newspapers published in the principal languages of that province and circulating therein. But this does not relieve a mutual insurance company from filing the balance sheet and profit and loss account with the Registrar of joint stock Companies of the province under s. 134 of the Indian Companies Act, 1913 or a co-operative life insurance society from filing such documents with the Registrar of co-operative societies of the province as he is required under the co-operative societies Act, 1912 or any other Provincial legislation.<sup>4</sup>

<sup>1</sup> Ibid, S. 98 (1).

<sup>2</sup> Insurance Act, 1938, S. 98 (2).

<sup>3</sup> Ibid, S. 99.

<sup>4</sup> Insurance Act, 1938, S. 100.

### **Supply of Documents to Members :**

Every Mutual Insurance Company and every Co-operative Life Insurance Society must furnish a copy of the document or documents filed with the Registrar of Joint Stock Companies or the Registrar of co-operative societies as the case may be to a member free of cost within fourteen days of the application made by the member in this behalf, provided the application is made by the member within two years from the date on which such document or documents are filed.<sup>1</sup>

### **Penalties :**

#### *Penalty for non-compliance with the provisions of the Act :-*

Any insurer who makes default in complying with or acts in contravention of any requirement of the Act and, where the insurer is a company, and director, managing agent, manager, or other officer of the company, or where the insurer is a firm, any partner of the firm who is knowingly a party to the default, is punishable with fine which may extend to Rs. 1000/- and in the case of a continuing default, with an additional fine which may extend to Rs. 500/- for every day during which the default continues.<sup>2</sup>

Any provident society which makes any default in complying with any requirement of the Act applicable to it and any director managing agent, manager, secretary, or other officer of the society who is knowingly a party to the default is punishable with fine which may extend to Rs. 500/- in the case of a continuing default with fine which may extend to Rs. 250/- for every day during which the default continues.<sup>3</sup>

### **Penalty for Non-compliance with the Requirements Regarding Capital and Deposit :**

But where the default is in respect of the requirements as to working capital and deposit, an insurer or any one acting on behalf of an insurer who transacts any class of insurance business in contravention of these requirements is punishable with fine

<sup>1</sup> Ibid. S. 101.

<sup>2</sup> Insurance Act, 1938, S. 102 (1).

<sup>3</sup> Ibid. S. 102 (2).

which may extend to Rs. 2000/-, and any one taking out a policy from an insurer or person who, to his knowledge, has contravened or continues to contravene these requirements is punishable with fine which may extend to Rs. 500/-<sup>1</sup>.

*Penalty for false statement in a document* :—Any person wilfully and knowingly making a false statement in respect of any material particular in any return, report, certificate, balance-sheet or other document required to be furnished under the Act, is punishable with imprisonment for a term which may extend to three years or with fine which may extend to Rs. 1000/- or with both.<sup>2</sup>

#### \* **Penalty for Wrongful Withdrawal or Withholding of Property :**

Any director, managing agent, manager or other officer of an insurer who wrongfully obtains possession of any property of the insurer or having any such property in his possession wrongfully withholds it or wilfully applies it for purposes not authorized by the Act is, on the complaint of the insurer or any member or policy-holder, punishable with fine not exceeding Rs. 1000/- and may be ordered by the Court to deliver up within a time the property so wrongfully obtained or withheld or misapplied and in default to suffer imprisonment for a term not exceeding two years.<sup>3</sup> In the case of liquidation of a provident society every officer, manager, proprietor or director of the society who withholds any property or books or assets from the liquidator when so required by the liquidator, will be punishable with imprisonment which may extend to six months, or with fine which may extend to Rs. 500/- or both and the court may order the delivery of the assets, or book or property to the liquidator.<sup>4</sup>

#### **Penalty for Wrongfully Diminishing Life Insurance Fund :**

Where an Insurance Company is in liquidation and the court is satisfied, on the application of the insurer or any member of the insurance company or any policy holder or the liquidator of the company, that by reason of any contravention of the provisions

<sup>1</sup> Ibid, S. 103 (1), (2).

<sup>2</sup> Insurance Act, 1938 S. 104.

<sup>3</sup> Ibid, S. 105.

<sup>4</sup> Ibid, S. 91 (2).

of the Act the amount of the life insurance fund has been diminished, every person who was at the time of the contravention a director, manager, liquidator or an officer of the company will be deemed guilty of misfeasance unless he proves that the contravention occurred without his consent or connivance and was not facilitated by any neglect or omission on his part. Any person guilty of such misfeasance may be proceeded against by the Court under secs. 235 and 237 of the Indian Companies Act and the Court has also the power to assess the sum by which the amount of the life insurance fund has been diminished by reason of the misfeasance and to order any person guilty thereof to contribute to that fund the whole or any part of that sum by way of compensation.<sup>1</sup>

*Sanction of the Advocate-General* —No proceeding against an insurer, or any director, manager or other officer of an insurer under this Act can be instituted by any person except the Superintendent of Insurance without the sanction of the Advocate General of the province in which the principal place of business of the insurer is situate.

*Relief by Court* —Where any person is liable in respect of negligence, default, breach of duty or breach of trust in relation to an insurer, the Court may relieve him of his liability on such terms as it thinks fit if it appears to the Court that he has acted honestly and reasonably and that having regard to all the circumstances of the case he ought fairly to be excused of his liability.<sup>2</sup>

*Cognizance of offences* —Only a Presidency Magistrate or a Magistrate of the first class can try any offence under the Act.<sup>3</sup>

<sup>1</sup> Insurance Act, 1938, S. 106.

<sup>2</sup> Ibid, S. 108.

<sup>3</sup> Ibid, S. 109.

## CHAPTER IX.

### MORTGAGE.

A mortgage is a transfer of an interest in specific *immovable* property for the purpose of securing payment of money advanced or to be advanced by way of loan, an existing or future debt, or the performance of an engagement which may give rise to a pecuniary liability. Thus, a mortgage may be (1) to secure a debt, or (2) to secure the performance of an engagement. (S. 58 of the Transfer of Property Act).

#### **Classes of Mortgage :**

Mortgages are of six kinds :—

(1) Simple mortgage, (2) Mortgage by conditional sale, (3) Usufructuary mortgage, (4) English Mortgage, (5) Mortgage by deposit of title deeds, and (6) Anomalous mortgage.

#### **(1) Simple mortgage :**

In a simple mortgage the mortgagor binds himself *personally* to pay the mortgage-money, and agrees, expressly or impliedly, that in the event of his failing to pay according to his contract, the mortgagee shall have a right to cause the mortgaged property to be sold and the proceeds of the sale to be applied in payment of the mortgage-money. In this kind of mortgage the mortgagor, however, remains in possession of the mortgaged property.

#### **(2) Mortgage by conditional sale :**

In this type of mortgage the mortgagor ostensibly sells the mortgaged property to the mortgagee on condition—

- (i) that on default of payment of the mortgage-money on a certain date the sale shall become *absolute*, or
- (ii) that on such payment being made the sale shall become void, or
- (iii) that on such payment being made the mortgagee shall re-transfer the mortgaged property to the mortgagor.

#### **(3) Usufructuary mortgage :**

In this kind of mortgage the mortgagor delivers or agrees to deliver the possession of the mortgaged property to the mortgagee,

and authorises him to collect the rents and profits accruing therefrom, and appropriate such rents and profits towards the payment of the principal money and interest owing on the mortgage debt.

**(4) English mortgage :**

Where the mortgagor binds himself to repay the mortgage money on a certain date, and transfers the mortgaged property absolutely to the mortgagee, but on condition that the mortgagee will re-transfer it to the mortgagor upon payment of the mortgage-money as agreed, the transaction is called an English mortgage.

An English mortgage is very similar to a mortgage by conditional sale. But there are fundamental differences between the two which may be stated as follows —

(a) In English mortgage the mortgagor binds himself to repay the loan on a certain day. But such an undertaking is not necessary in a mortgage by conditional sale.

(b) In English mortgage there is an absolute sale of the property at the outset and the ownership of the mortgagee is complete, only to be divested in case the mortgagor pays on the appointed date. But in a mortgage by conditional sale, the sale is complete only on default of the mortgagor to pay on the appointed date, and the ownership of the mortgagee is qualified, which may become absolute if the mortgagor defaults.

**(5) Equitable mortgage or mortgage by deposit of title deeds :**

Where a borrower borrows money by depositing title deeds of immovable property by way of security the transaction is called an equitable mortgage or mortgage by deposit of title deeds. In an equitable mortgage the following conditions must be satisfied —

(a) there must be delivery of title deeds to the creditor;  
 (b) there must be an intention to make the title deeds security for the loan

(c) the mortgage must be created in the towns of Calcutta, Bombay, Madras, Karachi, Rangoon and a few other towns.

**(6) Anomalous mortgage :**

Any mortgage which does not belong to any of the above classes is called an anomalous mortgage. The customary mortgages of India belong to this class.

**Rights of the mortgagor :**

A mortgagor has the following rights in respect of the mortgaged property :

1. He can, at any time after the mortgage debt has become due, get back the mortgaged property, provided he has paid or offered to pay the mortgagee the full amount of the mortgage debt. On such payment or offer of payment the mortgagee, if he is in possession must deliver the possession of the property to the mortgagor, and, if he has any documents of the mortgagor, he must return the same. This right of the mortgagor to get back his property is known as the equity of redemption. This right can never be destroyed even if the mortgagor contracts to give away this right.
2. Where the mortgagor has deposited his title deeds to the mortgagee he can inspect and make copies of the deeds at his own expense.
3. Where the mortgagee effects improvements on the mortgaged property while the property is in his possession the mortgagor is always entitled to the improvements. But the mortgagee can charge the cost of such improvement on the mortgagor, provided the improvement was necessary for preserving the property and preventing waste.
4. Where the mortgagee in possession of the mortgaged property renews the lease of the property, the mortgagor, on redemption of the property, becomes entitled to the renewed lease.
5. Where the mortgagee in possession of the mortgaged property makes additions to the property, the mortgagor, on redemption, becomes entitled to such accretion.

**Rights of the Mortgagee :**

The mortgagee has the following rights :—

- (1) He can obtain a decree for foreclosure against the mortgagor by which the mortgagor is deprived of his right of redemption and the mortgagee becomes the absolute owner of the

property. Foreclosure is granted only in case of mortgage by conditional sale where the mortgagor fails or neglects to pay the debt long after it becomes due.

(2) He can sell the property if the principal money with interest is not paid by the mortgagor after it has become due and he can realise his dues from the proceeds of the sale. In case of usufructuary mortgage and mortgage by conditional sale this right of sale cannot be exercised.

(3) He can sue for the mortgage money where—

- (a) the mortgagor has bound himself personally to pay the money, as in a simple mortgage
- (b) the mortgaged property has become insufficient to pay for the debt without the fault of either the mortgagor or the mortgagee,
- (c) the security whether property or title deeds has been partially or totally lost due to the mortgagor's fault,
- (d) the mortgagee is entitled to possession of the mortgaged property, as in mortgage by conditional sale or English mortgage, and the mortgagor is not giving him undisturbed possession

#### Hypothecation :

The mortgage of movable property is called hypothecation. Neither the Contract Act nor the Transfer of Property Act deals with the problem of hypothecation but it is well settled now that the mortgage of movable property, although unaccompanied by delivery of possession, is called hypothecation (*Deans v. Richard, son*, 1871, 3 N W P 54). It is also well settled that the hypothecate can enforce his claim even against a *bonsfide* transferee for value without notice of the hypothecate's claim. Thus in *Shyam Sunder v. Chitrabhanu* 1971, 3 W R 71 the hypothecate was allowed to enforce his security against a purchaser from the mortgagor or the hypothecator who had purchased the hypothecated goods for a value and without notice of the hypothecate's claim. It is submitted that this state of law in India is certainly very unsatisfactory. In the case of the mortgage of immovable property which can be created by registration only, any person dealing with the mortgaged property has automatically notice of the mortgage from the fact of registration, but in the case of mortgage of movable property, a third party can hardly know

himself of the mortgage since registration is not necessary. It is submitted that the law regarding hypothecation should be thoroughly overhauled in order to protect bonafide purchasers from fraudulent persons who deal with their property after having mortgaged the same without informing the purchaser of the same.

#### Lien :

Lien in its primary sense has been defined in Halsbury's Laws of England, as a right in one man to retain that which is in his possession belonging to another, until certain demands of the person in possession are satisfied. In this primary sense it is given by law and not by contract, for contract restricts a person's right to the stipulations in the contract. Such a lien is incidental to possession, but in exceptional cases such as in the case of liens for seamen's wages and Bottomry a lien may arise even without possession and may be enforced even against *bonafide* purchasers of the ship.

Lien is of two kinds, *viz.*, possessory and equitable.

#### Possessory lien :

Possessory lien is again of two kinds, *viz.* (a) General lien and (b) Particular lien. A general lien entitles a person in possession of goods to retain them until all claims or accounts of the persons in possession against the owner of the goods are satisfied. Such general lien has been established in the case of solicitors, bankers, factors, stock-brokers, warehouse-keepers and insurance brokers.

A particular lien, on the other hand, is a right to retain goods, until all charges incurred in respect of those goods only, have been paid. If the owner of the goods pays such charges, the goods cannot be retained until payment of the general balance due to the person having the particular lien. Thus a common carrier is under a legal obligation to carry goods and by way of compensation for such obligation, is entitled to retain the goods until the charge for carriage is paid. It has also been seen before that unpaid sellers have liens under particular circumstances.

#### Equitable Lien :

An equitable lien is an equitable right, conferred by law upon one man to a charge upon the real or personal property of another

until certain specific claims have been satisfied. Thus a vendor of land has an equitable lien on the land sold for the whole or part of the purchase money until actual payment.

#### Termination of lien :

A lien is terminated under the following circumstances :

- (a) Payment by the debtor of the amount due to the holder of the lien.
- (b) The abandonment of the claim for a number of years, or claiming to retain the goods on grounds different from those on which the creditor rests his claim for lien making no mention of the lien, or claiming the lien for a particular debt where the lien is for a general balance.
- (c) Acceptance of security by the creditor for the debt showing an intention to waive the lien.
- (d) Delivery of the goods to the owner or his agent. Once delivery is given to the owner, the lien cannot be revived, but if the owner takes possession by fraud the lien revives if possession is recovered.

#### Pledge :

This subject has already been dealt with under the Law of Contract.

#### Distinction between the different types of security mentioned above :

A mortgage differs from a hypothecation in that mortgage refers to immovable property whereas hypothecation refers to movable property. A mortgagee's right to sue is governed by the Transfer of Property Act and Order 34 of the Civil Procedure Code. But a hypothecatee's right to sue is not governed by any specific statute. His remedy is by way of a suit for sale of the property hypothecated and for declaration of charge in his favour. It has also been observed that hypothecation can be created without registration, whereas a mortgage cannot be created without registration.

A pledge comes nearest to hypothecation. But even then there are differences between the two. In pledge there must be

an actual or constructive delivery of possession of the goods pledged to the pledgee or pawnee, but in hypothecation the goods need not be delivered to the hypothecatee. A hypothecatee cannot sell the hypothecated goods without a decree of the court. But a pledgee can himself sell the goods pledged without a decree of the court, after giving a reasonable notice to the pawnor.

All the aforementioned securities differ from a lien in that the former are the creation of agreement between the parties whereas a lien is the creation of law under certain circumstances irrespective of the agreement of the parties. A lien is also only a defensive right and cannot be enforced by a suit or by sale of the properties over which the lien is claimed. The only right that the holder of a lien enjoys is to retain the goods until his dues are satisfied.

## CHAPTER X

### LAW RELATING TO CARRIAGE OF GOODS

#### Introduction :

Goods are carried by land, sea and air. There are rules of law which regulate such carriage of goods. They fix the liability, duty and rights of the consignor and the carrier. The inland transportation of goods is done by common carriers, private carriers, gratuitous carriers and the Railways. Prior to the passing of the Indian Carriers Act (III of 1865) and the Indian Railways Act (IX of 1890) the law relating to carriers in India was governed by the English common law relating to carriers<sup>1</sup>. The Indian Carriers Act (III of 1865) was passed with a view to limit the liability of common carriers imposed on them by the English common law and also to declare their liability for the negligence or criminal acts of themselves, their servants or agents<sup>2</sup>. The Indian carriers Act is largely based on the English Carriers Act, 1830. It applies to common carriers transporting goods for hire from place to place by land or inland navigation. Thus private carriers and carriers by sea are not affected by the Act. Even in the case of common carriers by land or inland navigation the Act does not displace the English common law altogether except in so far it limits the liability of such carriers in certain cases and precludes them from contracting out of their common law liability in the case of negligence and criminal acts of themselves or their agents. Thus the English common law so far as it is not modified by the Carriers Act, 1865 still regulates the duties and liabilities of such carriers in India<sup>3</sup>. The carriers Act, 1865 is now amended by two further Acts namely Act X of 1894 and Act XIII of 1921. Private carriers and gratuitous carriers were liable as under the English common law and their position must be the same in India<sup>4</sup>, their duties and liabilities being governed by the Indian

<sup>1</sup> Chagema *vs.* The Port Commissioner of Calcutta, 18 Cal. 427 . Mathura Kant Shaw *vs.* India General Steam Navigation Co., 10 Cal. 166 (181) F.B.; E. I. Ry. Co. *vs.* Jordan, 4 B.L.R.O.C. 97.

<sup>2</sup> Preamble to the Indian Carriers Act, 1865.

<sup>3</sup> Mothoora Kant Shaw *vs.* India General Steam Navigation Co., supra (per Mitter J.).

<sup>4</sup> Coggs *vs.* Bernard, 1 Sm. L.C. 175.

contract Act<sup>1</sup>. The duties and liabilities of railways were the same as those of common carriers under the English Law before the passing of the Railways Act (IX of 1890)<sup>2</sup>. But the Railways Act, 1890, has now limited their liabilities to those of a bailee.<sup>3</sup> The law relating to carriage of goods by sea in India continued to be governed by the English common law, unaffected by the carriers Act or the Railways Act, until the passing of the Carriage of Goods by Sea Act (XXVI of 1925) which now regulates the carriage of goods shipped from Indian ports under bills of lading. But even now carriage of goods by sea under a charter party or in respect of cases not covered by the Carriage of Goods by Sea Act, 1925, i.e., the rights and duties of the master, or the law relating to bottomry and respondentia or the question of salvage, would be governed by the common law of England.<sup>4</sup>

#### Kinds of Carriers :

The term 'carrier' is of very wide denotation and covers any one who carries goods or passengers whether for reward or not and is wide enough to include a railway owned and controlled by Government which takes upon itself the duty of carrying goods from one place to another<sup>5</sup>. Carriers are broadly divided into (a) carriers of goods and (b) carriers of passengers. Carriers of goods are again subdivided into (i) common or public carriers, (ii) private carriers and (iii) gratuitous or voluntary carriers<sup>6</sup>.

#### Common Carriers :

A common carrier has been defined by the Indian Carriers Act, 1865<sup>7</sup>, as a person including any association or body of persons whether incorporated or not, other than the Government, engaged in the business of transporting for hire property from place to place, by land or inland navigation, for all persons indiscriminately. We may set out the essential features of a common carrier as follows:—

(a) It may be a person, or a partnership or a joint family

<sup>1</sup> See the Law of Contract, supra.; S. 151, 152 & 161 of the Indian Contract Act.

<sup>2</sup> E. I. Ry. Co. vs. Jordan, supra.

<sup>3</sup> S. 72.

<sup>4</sup> Irrawaddy Flotilla Co. vs. Bhagwandas, L.R. 18 I.A. 121.

<sup>5</sup> Secretary of State vs. Golab Rai Paliram, L.R. (1937) 2 Cal. 614 (620).

<sup>6</sup> Hari Rao's Indian Railways Act, P. xii.

<sup>7</sup> Section 2.

business or a company. If it is a partnership firm all the partners will be jointly and severally subject to the liabilities of a common carrier. If it is a joint family business, all the members, adult and minor, will incur the liabilities of common carrier.

- (b) It must transport goods or property and not persons.
- (c) It must transport goods as a business and not merely as casual occupations.
- (d) It must transport goods for hire and not gratuitously.
- (e) It must carry goods indiscriminately for all i.e., for anyone who wants to employ it. It cannot choose to serve some people and refuse to serve others. A carrier who reserves the right of accepting or rejecting goods cannot be considered a common carrier<sup>1</sup>.
- (f) It must transport by land and inland navigation. Thus a carrier by sea is not to be regarded as a common carrier<sup>2</sup>.
- (g) It must not be the Government<sup>3</sup>.

It is clear, therefore, that many carriers who would be regarded as common carriers under the English law are not to be considered as such under the Indian carriers Act, e.g., carriers by sea or carriers of passengers.

#### Duties of a Common Carrier :

The duties of a common carrier may be set out as follows :—

- (1) A common carrier must carry the goods of all persons offering to pay a reasonable charge for carriage<sup>4</sup>. Unless, of course, the goods are not of the description which he professes or is accustomed to carry<sup>5</sup> or are of such nature as would expose him to exceptional danger<sup>6</sup>, or there is no accommodation for the goods<sup>7</sup>, or the

<sup>1</sup> Coggs *vs.* Barnard, 1 Sm.L.C. 12th Ed. 191.

<sup>2</sup> Mackillican *vs.* The Compagnie Des Messageries Maritimes De France, 6 Cal. 227.

<sup>3</sup> Alangir Footwear and Co. *vs.* Secretary of State, (1933) All. 466.

<sup>4</sup> Wylde *vs.* Pickford, (1841) 8 M. & W. 443.

<sup>5</sup> Great Western Railway *vs.* Sutton, (1868) 1 R. 4 H.L. 226; Oxlade *vs.* N. E. Ry. Co., (1860) 15 C.B.N.S. 680.

<sup>6</sup> Edwards *vs.* Sherratt, (1801) 1 East 604; G. N. Ry. Co. *vs.* L. E. P. Transport Co., (1922) 2 K.B. 742.

<sup>7</sup> Jackson *vs.* Rogers, (1863) 2 Show, 327.

goods are brought too late or too long a time before the journey is to begin.<sup>1</sup> If he refuses to carry the goods without justification (*i.e.*, except on the grounds mentioned above) he may be sued by the consignor of the goods. It was observed in *G. W. Ry. Co. v. Sutton*<sup>2</sup>, by Blackburn J., "The obligation which the common law imposed upon him was to accept and carry all goods delivered to him for carriage according to his profession (unless he had some reasonable excuse for doing so) on being paid a reasonable compensation for so doing : and if the carrier refused to accept such goods, an action lay against him for so refusing ; and if the customer, in order to induce the carrier to perform his duty, paid, under protest, a larger sum than was reasonable, he might recover back the surplus beyond what the carrier was entitled to receive, in an action for money had and received as being money extorted from him."

- (2) A common carrier must deliver the goods at the time agreed upon, or, where no time is stipulated within a reasonable time having regard to the circumstances of the case<sup>3</sup>.
- (3) A common carrier is bound to carry goods by the ordinary route which he professes to be his route<sup>4</sup>. But this need not be the shortest route<sup>5</sup>. He is, however, entitled to deviate from the ordinary route if that be necessary for the safe carriage of the goods and in that case the delay and deviation would be excused<sup>6</sup>.
- (4) A common carrier must deliver the goods to the consignee and to provide a place for their delivery. He will be liable for any loss arising from his neglect to do so<sup>7</sup>. But in the absence of agreement he is not bound to deliver the goods at the house of the consignee

<sup>1</sup> *Pickford v. Grand Junction Ry.*, (1844) 12 M & W. 166.

<sup>2</sup> (1869) L.R. 4 H.L. 236, 237.

<sup>3</sup> *Taylor v. Great Northern Railway*, (1855) L.R. 1 C.P. 385; *L. & N.W. Rail Co. v. Neikin*, (1922) 2 A.C. 263; *Dunn v. Bucknall Bros.*, (1902) 2 K.B. 614.

<sup>4</sup> *Foster v. G. W. Ry.*, (1904) 2 K.B. 306.

<sup>5</sup> *Hales v. London and North Western Railway*, (1863) 4 B. & S. 66.

<sup>6</sup> *Taylor v. G. N. Ry. Co.*, (1866) L.R.I.C.P. at p. 388.

<sup>7</sup> *Booth v. N. E. Ry. Co.*, L.R. 2 Ex. 195, 179.

and his liability ceases when he has brought the goods to the station of destination, and given to the consignee notice of arrival and allowed the consignee a reasonable time in which to remove the goods<sup>1</sup>.

### Rights of a Common Carrier :

The following are the rights of a common carrier :—

- (1) He is not bound to carry goods unless the sender is ready and willing to pay his reasonable charge or there is accommodation for the goods or the goods are of the description which he is accustomed to carry or the goods are not likely to subject him to exceptional danger<sup>2</sup>.
- (2) He is not bound to treat all customers equally and may at his option allow special concessions to some only. He is not, however, allowed to charge an unreasonable payment from any customer<sup>3</sup>. "The reasonableness of the charge must be measured by reference to the service rendered and the benefit received<sup>4</sup>, and this has to be determined without reference to the prosperity or misfortune of the parties to the contract<sup>5</sup>. But the fact that he charged other customers less may be evidence that a particular charge is unreasonable<sup>6</sup>.
- (3) He has a particular lien on the goods he carries in respect of his charges and he can retain the goods until his charges are paid<sup>7</sup>.

### Liability of a Common Carrier :

The liabilities of a common carrier in India are the same as under the English common law subject to the modifications introduced by the Carriers Act, 1865. Under the English common law a common carrier stands in the position of an insurer for the safe delivery of the goods intrusted to him for carriage and he is bound

<sup>1</sup> Mitchell *vs.* L. & S. Ry. Co., (1895) L.R. 10 Q.B. 256.

<sup>2</sup> See *supra*.

<sup>3</sup> G. W. Ry. Co. *vs.* Sutton, (1869) L.R. 4 H.L. 226 at 237.

<sup>4</sup> Canada Southern Ry. Co. *vs.* International Bridge Co., 8 A.C. 723 at 731, 732.

<sup>5</sup> Pr. Collins J., in Rickett Smith & Co. *vs.* Midland Ry. Co., (1896) I.Q.B. 260 at 265.

<sup>6</sup> Pr. Blackburn J., in G. W. Ry. Co. *vs.* Sutton, *supra*.

<sup>7</sup> Skinner *vs.* Upshaw, (1802) 2 Id. Raym. 752.

to indemnify the owner of the goods, whether the consignor or the consignee, for loss of or damage caused to the goods while in his custody irrespective of any question as to how such loss or damage was caused or whether he took all such reasonable care as a man of ordinary prudence would, under similar circumstances, take of his own goods. As the Privy Council observed in Irrawady Flotilla Co. *v.* Bhagwandas<sup>1</sup> "In England the liability of a common carrier for safe delivery of goods intrusted to his care has been always treated as independent of the contract to carry and was founded on common law and custom under which he is regarded as an insurer of the goods intrusted to his care." This has been held to be the law in India as well by a full Bench of the Calcutta High Court in Mathra Kant Shaw *v.* Indian General Steam Navigation Co.,<sup>2</sup> which was later on approved by the Privy Council in the case noted above<sup>3</sup>. It was further observed by the Full Bench in the above mentioned Calcutta case that the provisions in the Indian Contract Act relating to the liabilities of bailee<sup>4</sup>, had made no difference in the law on the subject.

Apart from the liabilities of an insurer, a common carrier may incur liability to the owner of the goods for any damage or loss which the latter may suffer in consequence of any breach of duty by the carrier even though the goods may have arrived safely e.g., if the owner suffers damage independently of any deterioration of the goods themselves owing to the delay in delivering the goods<sup>5</sup>. Thus where the plaintiff consigned certain books by railway for selection by a committee as text books for schools and the books did not reach the destination until long after such selection was made due to an extraordinary delay in transit so that the books became completely valueless for the plaintiff, it was held that the plaintiff was entitled to the price of the consignment by way of damages<sup>6</sup>.

The liability of a common carrier is, however, subject to certain

<sup>1</sup> 18 I.A. 121.

<sup>2</sup> 10 Cal. 166.

<sup>3</sup> Irrawady Flotilla Co. *v.* Bhagwandas, *supra*.

<sup>4</sup> 5a. 151 & 152.

<sup>5</sup> B. N. Ry. Co. & E. I. Ry. Co. *v.* Sheikh Dilu & Ors., A.I.R. (1925) Nag. 350.

<sup>6</sup> Secretary of State *v.* School Book and Apparatus Depot, A.I.R. (1933) Oudh, 339.

exceptions and modifications, some of which are recognised by the common law and some of which are statutory *i.e.*, imposed by the Carriers Act of 1865. We may note these exceptions below.

#### **Exceptions under the Common Law :**

The common law recognises certain exceptions which have the effect of either relieving the liability of the common carrier altogether in certain cases or of reducing such liability from that of an insurer to that of an ordinary bailee. These exceptions are as follows :—

- (1) A common carrier is relieved of liability altogether in case of loss of or damage to the goods intrusted to its care if such loss or damage is caused by (a) an act of God *e.g.*, a tempest, or (b) an act of the king's enemies *e.g.*, seizure, or destruction of the goods by enemies, or (c) the inherent vice or defect in the goods themselves *e.g.*, bad packing or deterioration by evaporation or breakage<sup>1</sup>. The position is correctly summarised by Lord Dredon in London and North Western Ry Co. *v.* Richard Hudson and Sons Ltd.,<sup>2</sup> in the following words—"That a common carrier is an insurer of goods entrusted to him for carriage and can only excuse himself on the ground of an act of God, or of inherent vice (in which expression I include bad packing) of the goods themselves is axiomatic."
- (2) A common carrier ceases to have the liability of an insurer after the goods arrive at their destination and he gives notice to the consignee of their arrival. If the consignee fails to take delivery of the goods or any part of them after such notice within a reasonable time, the carrier continues to have the liability of an ordinary bailee only in respect of the goods lying in his custody and will not be liable for any loss or damage unless the same is caused by his own negligence.<sup>3</sup> The carrier

<sup>1</sup> Hudson *vs.* Davendale, (1857) 27 L.J. Ex. 93; Nugent *vs.* Smith (1876) C.P.D. 423; Gould *vs.* S. E. & C. Ry., (1920) 2 K.B. 186; Great Northern Ry *vs.* L. E. P. Transport and Depository, (1922) 1 K.B. 742.

<sup>2</sup> (1920) A.C. 324 at p. 333

<sup>3</sup> Mitchell *vs.* Lancashire and Yorkshire Ry. Co., L.R. 10 Q.B.D. 256, 260.

may also expressly agree to store the goods on their arrival at the destination in which case also the liability of the carrier will be that of an ordinary bailee only.<sup>1</sup>

- (3) A common carrier may, by entering into special agreements with the consignor, exempt himself from liability for all loss and damage including those occasioned by his own negligence, or limit his liability to a particular kind or particular kinds of loss and damage. It is doubtful if a common carrier can, by a special agreement, relieve himself of liability for any loss caused by his own criminal act or that of his agents; for such an agreement would be void as against public policy or illegal. But the mere insertion of a general clause which exempts a carrier from liability for any loss or damage to the goods entrusted to him will not exempt a carrier from liability for any loss or damage occasioned by his own negligence or that of his servants or agents unless such exemption is expressly provided for in plain, express and unambiguous terms by inserting in the special agreement something equivalent to what is known as the negligence clause<sup>2</sup>. In England a special agreement limiting the liability of a carrier was provided for by carriers most frequently by inserting in newspapers, or distributing in hand-bills or, putting up in their offices a notice that they would not be liable for any property beyond a certain value, unless a special premium was paid for the insurance of the goods at the time of delivery. If this notice was brought to the knowledge of the consignor at the time the goods were delivered to the carrier, the consent of the consignor to the terms of the notice was implied and the carrier became entitled to the protection stipulated in the notice<sup>3</sup>. In order to avoid the strict common law liability of an insurer carriers were continually devising new types of agreements whereby they sought to reduce the liability of a carrier almost to nothing to the prejudice of the public.

<sup>1</sup> Van Sall *vs.* S. E. Ry. Co., (1862) 31 L.J.C.P. 241.

<sup>2</sup> Price & Co. *vs.* Union Lighterage Co., (1904) 1 K.B. 412.

<sup>3</sup> Mayhew *vs.* Eames, (1825) 3 L.J. (O.S.) K.B. 108; Nichols v. Willam, (1804) 5 East 507.

The carriers Act of 1865 was, therefore, designed to relieve the strict liability of carriers as well as to restrict their powers to make one-sided special contracts.<sup>1</sup>

#### Exceptions under the Carriers Act :

The carriers Act of 1865 affects the common law liability of a carrier as follows. For the purpose of defining the liabilities of a common carrier it divides articles which may be consigned into two categories, namely (1) the Scheduled articles and (2) the non-scheduled articles. The scheduled articles are those enumerated in the schedule to the Act and which are unusually valuable or unusually perishable,<sup>2</sup> i.e., gold, silver, jewellery, silk, paintings, engravings, title deeds, currency notes or coins, bills, hundis and etc. The non-scheduled articles are those which are not included in the schedule to the Act and which are of an ordinary kind e.g., wheat and rice and not unusually valuable or perishable.<sup>3</sup>

(1) As regards the scheduled articles the carriers Act, 1865 prescribes the liability of a common carrier as follows :—

(a) A common carrier is not liable for any loss of or damage to a scheduled article exceeding Rs. 100/- in value excepting when it is caused by a criminal act of the carrier, his servants, or agents, unless the value and description of the article is declared by the consignor or his duly authorised agent at the time when the goods are delivered to the carrier whether such loss or damage is caused by the negligence of the carrier or not.<sup>4</sup> In *Narang Rai Agarwalla v. River Steam Navigation Co., Ltd.*<sup>5</sup> the plaintiff sued the River Steam Navigation Co., Ltd., for the loss of a few bundles of Endi silk (which is a scheduled article), delivered to it at Guwahati for transmission to Calcutta via E. B. Ry. The amount of loss exceeded Rs. 100/- in value. It was held that the River Steam Navigation Co., was

<sup>1</sup> Vide Sir Henry Maine's speech before the India Council in introducing the Carriers Bill in the *Gazette of India*, suppl., 2-12-1864.

<sup>2</sup> Vide Sir Henry Maine's Speech, *Ibid.*

<sup>3</sup> Vide Sir Henry Maine's Speech, *Ibid.*

<sup>4</sup> Carriers Act, 1865, Ss. 3 & 8.

<sup>5</sup> 11 C.W.N. 1071.

not liable for the loss as the plaintiff failed to declare the value and description of the goods at the time of delivery.

- (b) A common carrier is allowed to charge an additional rate for undertaking the increased risk of carrying a scheduled article provided a scale of charges containing the additional rate is publicly exhibited in his place of business in English as well as the vernacular language of the place<sup>1</sup>.
  - (c) A common carrier is liable for any loss of or damage to a scheduled article entrusted to him for carriage and is bound to return any sum which might have been paid as the charge for carriage, where the consignor or his agent has properly declared the value and description of the article and has paid or agreed to pay the increased rate, if any, and the carrier cannot limit his liability in this respect by any special agreement<sup>2</sup>.
- (2) As regards non-scheduled articles, a common carrier may limit his liability for the loss of or damage to goods, entrusted to his care, by special contracts signed by the owner or his duly authorised agent excepting when such loss or damage is caused by the negligence or criminal act of the carrier or any of his agents or servants<sup>3</sup>. As Sir Lawrence Jenkins observed in *British and Foreign Marine Insurance Co., Ltd. v. India General Navigation and Railway Co., Ltd.*,<sup>4</sup> "the liability of a common carrier for the loss of goods, not being of the description contained in the Schedule, may be limited by special contract signed by the owner, save when such loss shall have arisen from the negligence or criminal act of the carrier or any of his agents or servants." It is clear that any special agreement which purports to exempt the carrier from liability for his own negligence or criminal act or that of his servants or agents is void

<sup>1</sup> Carriers Act, 1865, S. 4.

<sup>2</sup> *Ibid.*, Ss. 3 & 6; *British and Foreign Insurance Co. Ltd. v. India General Navigation and Ry. Co. Ltd.*, 38 Cal. 28 (42).

<sup>3</sup> Carriers Act, Ss. 6 & 8.

<sup>4</sup> 38 Cal. 28.

and unoperative as being illegal and in contravention of the carriers Act<sup>1</sup>. In India General Steam Navigation Co. v. Joy Kristo Saha,<sup>2</sup> the defendant I. G. S. N. Co., received the goods of the plaintiff for carriage under conditions contained in a forwarding note signed by the plaintiff. One of such conditions stipulated that the defendants would not be liable in the case of loss or damage arising from certain kinds of accidents and also from the negligence of the defendants. The goods were lost as a result of the flat carrying the goods being sunk by collision with an underwater snag, the existence of which could not have been ascertained by any precautions on the part of the defendants. It was held that the defendants could limit their liability by special agreement as the goods were not of the scheduled class but not so as to relieve them of their liability for their own negligence and that the condition which purported to do so was, therefore, bad. On the facts, however, it was held that the defendants were not liable as the loss was due to one of the excepted conditions which were severable from the condition which was bad and not due to the negligence of the defendants.

#### **Carriers Act, how far it modifies the Liability of a Common Carrier under the Common Law :**

As regards scheduled articles whose value and description have been declared, the liability of a common carrier under the carriers Act, 1865 is absolute and higher than that under the common law for he cannot limit his liability by any special agreement, nor can he, it seems, claim protection under any of the common law exceptions e.g., an act of god or an act of the king's enemies. As regards scheduled articles whose value and description have not been declared the liability of a common carrier is much lighter than that under the common law for he is only liable if the loss or damage does not exceed Rs 100/- in value or if the loss or damage is caused by his criminal act or that of his agents. It is not clear as to what the liability of a common carrier would be in the case

<sup>1</sup> Carriers Act, 1865, S 8, River Steam Navigation Co Ltd. vs Jamunadas Ramkumar, 59 Cal 472 (474)

<sup>2</sup> 17 Cal 39

of loss or damage not exceeding Rs. 100/-, in respect of scheduled articles whose value and description have not been properly declared. It seems that the liability of the carriers would be absolute unless the articles are consigned as ordinary or non-scheduled articles under special agreements.

As regards non-scheduled articles the liability of a common carrier is the same as under the common law excepting that he cannot contract out of his liability for loss or damage caused by his negligence by any special agreement which is permissible under the common law.

#### Presumption of Negligence :

Under the Carriers Act, 1865, a common carrier is liable absolutely for any loss or damage caused by his negligence excepting in the case of scheduled articles whose value and description have not been properly declared and, as we have seen, he cannot limit this liability by any special agreement<sup>1</sup>. Where in a suit brought against a common carrier, the common carrier wants to relieve himself from liability for the loss or damage for which he is sued under any special agreement, it is for him to prove the absence of negligence<sup>2</sup>. The burden of proof of absence of negligence is thus thrown on the common carrier on the principle that the loss or damage to the goods is *prima facie* proof of negligence and the Court must presume negligence in the absence of any proof to the contrary<sup>3</sup>.

#### Suits against a Common Carrier :

Any person who has an interest in the goods consigned and suffers loss of or damage to the goods can maintain a suit against the common carrier to whom the goods were entrusted for carriage whether he was a party to the contract of carriage or not or in the language of law whether there was privity between him and the carrier or not<sup>4</sup>. The reason is explained by the Privy Council in Irrawady Flotilla Co. *v.* Bhagwandas<sup>5</sup>, in the following words

<sup>1</sup> S. 8 ; I. G. S. N. Co. *v.* Joy Kristo Saha, 17 Cal. 39 ; R. S. M. Co. Ltd. *v.* Jamunadas Ramkumar, 59 Cal. 472.

<sup>2</sup> Carriers Act, 1865, S. 9.

<sup>3</sup> The River Steam Navigation Co. *v.* Choutmull Dougur, 26 Cal.

<sup>4</sup> K. C. Dhar *v.* Ahmed Buz, 60 Cal. 879 at p.

<sup>5</sup> 18 L.A. 121 at p. 129.

"The obligation imposed by law on common carriers has nothing to do with contract in its origin. It is a duty cast upon common carriers by reason of their exercising a public employment for reward. 'A breach of this duty,' says Dallas C. J. (*Betherton v. Wood*)<sup>1</sup> is a breach of the law, and, for this breach, an action lies founded on the common law, which action *wants not the aid of a contract to support it.*" Thus a consignee to whom the property in the goods has passed or a mortgagee of the goods or even an insurer who has paid the owner for the loss of the goods<sup>2</sup>, can maintain an action against the carrier for loss or damage to the goods.

*Requirement of notice* :—No suit can be instituted against a common carrier for the loss of, or injury to, goods entrusted to him for carriage unless notice in writing of the loss or injury has been given to him before the institution of the suit and within six months of the time when the loss or injury first came to the knowledge of the plaintiff<sup>3</sup>. Notice to a local agent of the carrier is valid notice even though such local agent may also be the agent for another carrier<sup>4</sup>.

*Limitation* :—A suit against a carrier, which includes a common carrier, for compensation for loss of or injury to goods must be instituted within one year of the time when the loss or injury occurs and a suit for compensation for non-delivery of or delay in delivery of the goods must be instituted within one year of the time when the goods ought to be delivered<sup>5</sup>.

#### Private Carriers :

A private carrier has been defined by Avory J. in *Watkins v. Cottell*<sup>6</sup> as one whose trade is not that of conveying goods from one person or place to another, but who undertakes upon occasion to convey the goods of another and receives reward for so doing. A private carrier differs from a common carrier in that he is

<sup>1</sup> (1821) 3 Brod. & B., 54.

<sup>2</sup> *British & Foreign Marine Insurance Co. Ltd. vs. I. G. N. & Ry. Co. Ltd.*, 38 Cal. 28.

<sup>3</sup> *Carriers Act, 1865*, S. 10; *R. S. N. Co. Ltd. vs. Kashi Prasad*, 8 C.L.J. 192.

<sup>4</sup> *India General Navigation & Ry. Co. vs. Girdharilal Gobardhan Das*, 54 Cal. 430.

<sup>5</sup> *Limitation Act, Articles 30 & 31.*

<sup>6</sup> (1916) 1 E.R. 10 at p. 14.

either one (a) who undertakes to carry for reward on occasions but not as a public employment or (b) one who, while inviting all and sundry to employ him as a carrier for reward, reserves the right to accept goods at his option<sup>1</sup>

### **Liability of a Private Carrier :**

The liability of a private carrier is like that of a bailee. He is liable only for such loss or damage as is caused by his negligence i.e., by his failure to take as much care of the goods entrusted to him as a man of ordinary prudence would, under similar circumstances, take of his own goods<sup>2</sup>. But a private carrier is not liable if the owner keeps the goods under his control e.g. when a passenger carries his own luggage or if the loss is as likely to have arisen from the misconduct of the owner or his want of care, as from that of the carrier.

### **Gratuitous Carrier :**

A person who undertakes to carry goods or passengers gratuitously i.e. without reward, is called a gratuitous carrier. No action can be maintained against a gratuitous carrier for refusing to carry goods or passengers after he has undertaken to do so for the contract is *nudum actum* i.e. unenforceable for want of consideration<sup>3</sup>. But once a gratuitous carrier accepts goods for carriage he is in the position of a bailee and his liabilities become the same as that of a private carrier, i.e., he will be liable for any loss or damage caused by his own negligence or that of his agents. As Wills J observed in *Skelton v L & N W Ry Co*<sup>4</sup> "If a person undertakes to perform a voluntary act, he is liable if he performs it improperly but not if he neglects to perform it. Such is the result of the decision in *Coggs v Bernand*"

### **Carriers of Passengers :**

Carriers of passengers may be either (a) a common carrier or (b) a private carrier or (c) a gratuitous carrier. The Carriers Act,

<sup>1</sup> *Belfast Ropework Co vs Rushell* (1918) 1 K.B. 210

<sup>2</sup> Contract Act, Ss. 151 & 152, *Coggs vs Bernand* 1 Sim. L.C. 12th ed.

<sup>3</sup> *Whalley vs Wray*, 3 E.P. 74

<sup>4</sup> *Coggs vs Bernand*, *supra*

51 R. 2 C.P. 636

1863, does not affect their position as under the common law which still governs them. We shall discuss their position below.

*Common carrier of passengers* :—A person who is engaged in carrying passengers as a regular business and who holds himself out as ready to carry between places on a certain route all persons indifferently who accept his published terms is a common carrier of passengers<sup>1</sup>. He is regarded as a common carrier because he is bound to carry any member of the public who wants to travel unless he can justify his refusal to do so under any one of the following common law exceptions, namely, (a) where the person offering himself to be carried is unfit or (b) where such person is unwilling to pay the stated fare or (c) where there is no accommodation. A bus company, or a tramway company which carries every one indiscriminately may be regarded as common carriers.

The liability of a common carrier of passengers is different to that of a common carrier of goods in that he does not stand in the position of an *insurer* for the safety of the passengers he carries. He does not warrant that the carriage in which the passengers travel is free from all defects likely to cause peril, although those defects may be such that no skill, care, or foresight could have detected their existence<sup>2</sup>.

His duty is only to take due care and exercise due diligence in carrying the passengers and he will be held liable only in case of his negligence, i.e., if injury is caused to a passenger by any defect which could have been detected by the exercise of reasonable care and diligence e.g., where a passenger is injured by the tender of the train being thrown off the line as a result of a defect in the tyres of one of the wheels of the tender<sup>3</sup>. Thus Sir James Mansfield observed in *Christie v. Griggs*,<sup>4</sup> "there is a difference between a contract to carry goods and a contract to carry passengers. For the goods the carrier was liable at all events, but he did not warrant the safety of the passengers. His undertaking as to them went no further than this, that *as far as human care and foresight could go* he would provide for their safe conveyance."

<sup>1</sup> The liability of a common carrier for passengers is the same

<sup>2</sup> *Hari Rao's Indian Railways Act*, p. 734.

<sup>3</sup> *Readhead v. Midland Ry. Co.*, (1869) 4 Q.B. 379 at 389.

<sup>4</sup> *Ford v. London and South Western Rly. Co.*, 2 F. & F. 730.

<sup>4</sup> 2 Camp. 79.

in relation to passengers who travel free or without ticket as that for passengers who travel with ticket provided the former does so with the knowledge and consent of the carrier.<sup>1</sup> But if a passenger travels free without the knowledge and consent of the carrier, he is regarded as a mere trespasser and the carrier is not liable for any injury caused to him whether by negligence of the carrier or not. In *G. N. Ry. Co. v. Harrison*<sup>2</sup> a newspaper reporter held a free railway ticket in his own name. Another reporter, while travelling with the former's free ticket, was injured. The railway had knowledge of a practice whereby one reporter frequently travelled with another's ticket and had permitted the same. It was held that the injured reporter was entitled to recover damage for his injury as he was no trespasser, his irregular user of the railway having been permitted by the railway.

A common carrier of passengers is not liable for the injury caused to any passenger where the injury is caused as much by the negligence of the passenger as of the carrier<sup>3</sup>.

*Private Carrier of passengers* :—A person who carries passengers for reward on occasions or who, while inviting all and sundry for the purpose of being carried, reserves the right to refuse to carry anyone at his option is to be deemed a private carrier of passengers<sup>4</sup>. His liability is the same as that of a common carrier of passengers.

*Gratuitous carrier of passengers* : A person who undertakes to carry anyone gratuitously i.e., without reward is to be regarded a gratuitous carrier. He is not bound to carry anyone but once he does carry anyone he will be liable if an injury is caused to the latter by his negligence.

#### Railways whether Common Carriers :

In India the railways stand on a different footing as compared to common carriers so far as their liabilities are concerned. Under

<sup>1</sup> *G. N. Ry. Co. vs. Harrison*, 23 L.J. Ex. 308 (310).

<sup>2</sup> *Supra*.

<sup>3</sup> *Jehangir Muncherji vs. B. B. & Co. I. Ry. Co.*, 37 Bom. 575. In this case a passenger injured his arm by projecting it out of the window of a running train and colliding against the door of a stationary train which was kept open by the carrier negligently. It was held that the passenger was as much negligent by projecting his arm—as the carrier.

<sup>4</sup> *Per Avery J.*, in *Watkins vs. Cottell*, (1916) 1 K.B. 10 at 14.

S. 72 of the Railways Act, 1890, the liability of railways is defined to be that of a bailee as laid down in Ss 151, 152 and 161 of the Contract Act, and not that of an insurer as under the common law in respect of the loss, deterioration or destruction of goods and animals carried by them. But although a railway company is not a common carrier so far as its liability is concerned, yet it is regarded as a common carrier so far as its duties to the general public are concerned. Thus it cannot refuse to carry goods tendered to it without the justification recognised in common law<sup>1</sup> or make unreasonable delay in delivering the goods or refuse to deliver them without justification. As Staples, A.C.J. observes in *Chhogal vs. Secretary of State*, 'When once a railway company has held itself out to be a common carrier, it is under a common law liability to carry goods to all places to which it professes to carry and to accept all goods which are reasonably offered to it for conveyance to and from the places to which it professes to carry'. A similar view was expressed by Walsh J in *Sohan Pal vs. E. I. Rly Co*<sup>2</sup> in the following words "A railway company is by law a common carrier. It cannot lawfully refuse to carry goods properly tendered to it. It is given statutory existence and wide statutory powers in exchange for public duties and it is bound to carry goods".

Even as regards the liability of a railway company, a railway company has been held liable as a common carrier for any damage suffered by the owner of the goods which has been occasioned by reason of any breach of common law duty by the carrier excepting when such damage is caused by the loss, destruction or deterioration of the goods. The liability of a railway company is like that of a bailee only when such liability arises from the loss, destruction or deterioration of the goods or animals carried by it and no otherwise. Thus the liability of a railway for non-delivery of goods which have not been lost or damaged or for undue delay in delivering goods or for injury to the persons of passengers would not be governed by the Railway Act, 1890, but by the common law<sup>3</sup>.

<sup>1</sup> See *supra*

<sup>2</sup> *Paxi Ellahi vs. E. I. Ry Co*, 43 All 623

<sup>3</sup> A.I.R. (1933) Nag 262 at p. 262

<sup>4</sup> 44 All. 218 at 227 (F.B.).

<sup>5</sup> *East India Ry Co vs. Jogpat Singh*, 51 Cal. 615.

### **Liability of Railways :**

In India the liability of a railway administration for the loss, destruction or deterioration of animals or goods delivered to it for carriage is not like that of an insurer under the common law but like that of a bailee under Ss. 151, 152 and 161 of the Contract Act.<sup>1</sup> The duty of a railway administration is to take reasonable care only and it will be liable for the loss, destruction or deterioration of goods or animals entrusted to it in the following cases only :—

- (a) If the goods or animals are lost or damaged owing to the neglect of the railway or its servants to take such reasonable care as a man of ordinary prudence would, under similar circumstances, take of his own goods.<sup>2</sup>
- (b) If the goods or animals are lost or damaged for any reason after the railway has made default in delivering the goods or animals at the proper time.<sup>3</sup>

But this general liability of a railway as a bailee is further limited in the following cases, namely (a) carriage of articles mentioned in the second schedule to the Railways Act, 1890, (b) carriage of animals, (c) carriage of passenger's luggage and (d) carriage under special agreements known as *risk notes*.

- (a) *Carriage of Articles mentioned in the second schedule to the Act* :—A railway administration is not liable for the loss, destruction or deterioration of any parcel or package, containing any article of special value mentioned in the second schedule to the Railways Act e.g., gold, silver, silk pearls, jewellery, watches, Government and other securities, paintings, engravings and etc., the value whereof exceeds Rs. 100/- unless the person sending or delivering the same declare the value and contents thereof at the time of the delivery of the package or parcel to the railway for carriage and paid or agreed to pay an additional rate as insurance against the extra risk of carrying the same, if so required by the railway. If the consignor does not declare the value and contents of a package containing such article exceeding Rs. 100/- in value or does not pay the

<sup>1</sup> Railways Act, 1890, S. 72(1).

<sup>2</sup> Contract Act, Ss. 151 & 152.

<sup>3</sup> Ibid, S. 161.

additional rate when required by the railway, he cannot recover any loss or damage even though it may be caused by the negligence of the railway or its servants.<sup>1</sup> Where such value and contents have been declared the railway is liable to pay upto the declared value if any loss or damage occurs, but the burden of proving the extent of the loss or damage is upon the person who claims compensation.<sup>2</sup> A railway may, before accepting any parcel or package declared to contain such an article examine the contents of the parcel or package in order to ascertain that it really contains such an article.<sup>3</sup> When a consignor sends any such article declared as such without paying the additional rate the practice of a railway is to take from the consignor an agreement in risk note Form called X or Y whereby the consignor agrees to absolve the railway of all liability in consideration of the articles being carried at the ordinary rate.

A specimen form in which the consignor has to make a declaration as to the value and contents of a package containing such an article is given below :—

**FORM OF DECLARATION UNDER S. 75.**

**Declaration to be signed by the vendor of excepted articles.**

### The accompanying

### **weighing**

**address to**

**contains the articles detailed below of the aggregate value of Rs.**

(in words)

**Rs.**      **As.**

**Dated**

19

*Signature of Sender.*

Parcels or goods must be securely packed in a manner approved by the Station Master before they are accepted for despatch. Articles packed in cloth should bear seals (at intervals not exceeding 3 inches along each line of sewing) showing distinct impressions of some device other than that of current coin.

The Railway reserve the right to open packages containing excepted articles to ascertain that the articles are sound and in good condition. All appliances in packing, etc., must be provided by the sender or receiver, who will see and be responsible that the packages are properly packed and re-packed.

<sup>1</sup> Railway Act, 1890, s. 75 (1).

<sup>2</sup> Ibid, S. 75 ((2).

<sup>2</sup> Ibid, S. 75 (3).

## DESCRIPTION OF CONTENTS

Description.	No. of Articles.	Weight	Value	Remarks
	Mds	Srs.	Rs.	A. P.

*Insurance is optional with senders*

(b) *Carriage of Animals* —The liability of a railway administration as a bailee, for the loss of or damage to animals delivered to it cannot in any case exceed, in the case of elephants or horses, Rs 500/- a head or, in the case of mules, camels or horned cattle, Rs 50/- a head or, in the case of donkeys, sheep, goats, dogs or other animals, Rs 10/- a head unless the person sending or delivering them to the railways declares at the time of delivery that they were respectively of higher value than Rs. 500/-, Rs 50/-, or Rs 10/- a head as the case may be.<sup>1</sup> Where such higher value has been declared the railway may charge an additional rate as insurance against the extra risk involved in their carriage.<sup>2</sup> In case of any loss or injury to an animal delivered to the railway for carriage, the burden of proving the value of the animal or the extent of the injury is on the person who claims compensation.

for

<sup>1</sup> Railways Act, 1890, S. 73 (1).

<sup>2</sup> Ibid, S. 73 (2).

pensation for such loss or injury.<sup>1</sup> It should be noted, however, that the railway will be liable as a bailee only when such loss or injury results from the negligence or misconduct of the railways or its servants and if the animal dies or gets injured from its own inherent vice e.g., where it jumps out of a truck and kills itself or kicks about and injures its legs. But the onus of proving absence of negligence is on the railway where it is proved that the animal which dies or gets injured was fit and healthy at the time it was loaded in a truck.

(c) *Carriage of Passengers' Luggage*. —A railway administration is not liable for the loss, destruction or deterioration of any luggage belonging to or in charge of a passenger unless a railway servant has booked and given a receipt therefor. This means that to hold a railway liable for the loss of a passenger's luggage the first requisite is that the passenger must have booked it and obtained a receipt thereof. But it does not follow that the railway is liable in every case of loss or damage to a passenger's luggage. Its liability in this respect is also like that of a bailee and will arise only if the loss or damage is caused by its own negligence or misconduct or that of its servants.<sup>2</sup> Thus if the passenger takes his luggage completely out of the control of the railway e.g., by keeping it in his compartment and the luggage is lost by his own negligence the railway will not be liable for the loss.<sup>3</sup>

(d) *Carriage under special agreements or risk note*. —A railway administration can limit its liability even as a bailee by entering into a special agreement with the consignor or his duly authorised agent. Such a special agreement, in order to be effective, must be in writing signed by or on behalf of the person sending or delivering the goods to the railway and must be in a form approved by the Governor-General in Council.<sup>4</sup> Special agree-

<sup>1</sup> Ibid, S 73 (3).

rep. <sup>2</sup> Blower *vs.* G W Ry Co, (1887) 4 T.L.R. 7

<sup>3</sup> Smith *vs.* Midland Railway Co, 57 L.T. 813

<sup>4</sup> *Met Hussain  B. & N W Ry Co, 13 C.W.N. 847*

<sup>5</sup> Railway *vs.* Southampton Steam Packet Co, (1919) 2 K.B. 135

<sup>6</sup> Ibid, S 75 (5).

<sup>7</sup> Ibid, S 75 (2) (a) & (b).

ments of this kind are known as risk notes and they purport to exempt the railway from even the liability of a bailee under certain conditions in consideration of the railway granting the consignor some concession in the shape of charging him a reduced rate of freight. There are several kinds of risk notes which have been approved by the Governor-General in Council and which are in current use, namely, risk notes A, B, C, D, E, F, G, H, X and Y. Risk notes C, X and Y exempt the railway from liability in every case of loss and damage, however caused. Risk notes A, B, D, G and H absolve the railway of liability for any loss or damage excepting where it is caused by the misconduct of the railway's servants. Risk notes E. and F limit the liability of the railway to specified sums agreed to as the maximum payable by the railway in respect of loss of or damage to certain classes of animals carried under the notes and relieve the railway of liability to pay even limited sums unless the loss or damage is caused by the negligence or misconduct of the railway company or that of their servants. We may study these risk notes in detail below :—

#### Risk note "A" :

When goods which are tendered to a Railway for carriage are either in bad condition or so defectively packed as to be liable to damage, leakage or wastage in transit the practice of the railway is to take an agreement from and signed by the person delivering in risk note form "A", the effect of which is to relieve the Railway of all liability for any condition in which the goods may be delivered to the consignee or for any loss or damage excepting when such loss or damage is caused by the misconduct of the Railway's servants. The form of Risk note "A" is given below :—

#### NEW RISK NOTE FORM A.

[Approved by the Governor-General in Council under section 72 (2) (b) of the Indian Railways Act, IX of 1890]

(To be used when articles are tendered for carriage which are either in bad condition or so defectively packed as to be liable to work, leakage or wastage in transit.)

STATION  
193

tendered by—  
us

Whereas the consignment of \_\_\_\_\_ per Forwarding Order No \_\_\_\_\_ of \_\_\_\_\_ by the \_\_\_\_\_ Railway Administration to \_\_\_\_\_ under Railway Receipt No \_\_\_\_\_ of \_\_\_\_\_ [date] is in bad condition and \_\_\_\_\_ liable to damage, leakage or wastage in transit as follows:—

1

\_\_\_\_\_, the undersigned, do hereby agree and undertake to hold the said We

Railway Administration over whose Railway the said goods may be carried in transit from \_\_\_\_\_ station to \_\_\_\_\_ station harmless and free from all responsibility for the condition in which the aforesaid goods may be delivered to the consignee at destination and for any loss arising from the same except upon proof that such loss arose from misconduct on the part of the Railway Administration's servants

This agreement shall be deemed to be made separately with all Railway Administrations or transport agents or other persons who shall be carriers for any portion of the transit

WITNESS (Signature)	Rank of (Residence)	Signature of sender Father's name
WITNESS (Signature)	Caste	Age
(Residence)	Profession Residence	

It should be noted that though attestation by witness is provided for in risk note A, yet it is not essential<sup>1</sup>. The onus of proving misconduct on the part of the Railways servants is on the person who claims compensation for any loss or damage<sup>2</sup>. Misconduct is not negligence. It is some positive act or some wilful omission to do something which it is the duty of the Railways to do and is opposed to accident or negligence.

### RISK NOTE "B"

When a consignor sends goods or animals at a "special reduced or "owne's risk rate" instead of an alternative "ordinary" or "risk

re.—

<sup>1</sup> Ardesir Bhukap Tamboli v. G I P Ry Co, 52 Bom. 169 (174).

<sup>2</sup> R.R. & S. M. Ry Co Ltd v. Ravi Singh Deepaung, A.I.R. (1995) 811 and 812.

<sup>3</sup> Ibid, S. 75 Dangra v. The Governor General in Council, 48 C.W.N. 554.

<sup>4</sup> Ibid, S. 75 (1).

"acceptance" rate, the practice of the Railway Administration to which the goods or animals are delivered for carriage is to accept the goods or animals under an agreement in risk note form B signed by the sender which exempts the Railway from all liability for any loss of or damage to the goods or animals excepting when such loss or damage is caused by the misconduct of the Railway's servants. The burden of proving misconduct of the Railway's servants in case of any loss or damage is on the person who claims compensation. But in the case of non-delivery of the whole of a consignment or of the whole of one or more packages forming part of the consignment not due to fire or accident or in the case of pilferage from such package or packages, the Railway administration must in the first instance disclose how it dealt with the consignment and, if necessary, to give evidence thereof before the consignor is called upon to prove misconduct. If from such disclosure misconduct cannot be inferred the person claiming compensation must prove misconduct. The form of Risk Note "B" is given below :

## **NEW RISK NOTE FORM B :**

[Approved by the Governor-General in Council under section 72 (2) (b) of the Indian Railways Act, IX of 1890.]

(To be used when the sender elects to despatch at a "special reduced" or "owner's risk" rate, articles or animals for which an alternative "ordinary" or "risk acceptance" rate is quoted in the Tariff.)

STATION.  
193

Whereas the consignment of the  
tendered by us as per Forward  
us  
ing Order No of (date) for despatch by the  
Railway Administration to station, under Railway Receipt  
No of (date) is charged at a special reduced rate  
instead of at the ordinary tariff rate chargeable for such consignment,

the undersigned, do, in consideration of such lower charge agree and undertake to hold the said Railway Administration harmless and free from all responsibility for any loss, destruction or deterioration of, or damage to, the said consignment from any cause whatever except upon proof that such loss, destruction, deterioration or damage arose from the misconduct of the Railway Administration's servants; provided that in the following cases:—

- (a) Non-delivery of the whole of the said consignment or ~~any~~  
whole of one or more packages forming part of the ~~work~~  
consignment packed in accordance with the instruction  
in the Tariff or, where there are no such,

tected otherwise than by paper or other packing readily removable by hand and fully addressed, where such non-delivery is not due to accidents to trains or to fire; .

- (b) Pilferage from a package or packages forming part of the said consignment properly packed as in (a), where such pilferage is pointed out to the servants of the Railway Administration on or before delivery;

the Railway Administration shall be bound to disclose to the consignor how the consignment was dealt with throughout the time it was in its possession or control and, if necessary, to give evidence thereof before the consignor is called upon to prove misconduct, but, if misconduct on the part of the Railway Administration or its servants cannot be fairly inferred from such evidence, the burden of proving such misconduct shall be upon the consignor.

*This agreement shall be deemed to be made separately with all Railway Administration or transport agents or other persons who shall be carriers for any portion of the transit.*

WITNESS	Signature of sender		
(Signature)	Father's Name		
(Residence)	Rank or {	Caste	Age
WITNESS.			
(Signature)	Profession		
(Residence)	Residence		

(To be filled in by Booking Clerk.)

Description of packing	Booking Clerk.
Date	1

### RISK NOTE "C"

When goods, which should normally be carried in covered wagons, carts or boats and which are liable to damage if not so carried, are accepted for carriage in open wagons, carts or boats at the sender's request, the Railway Administration to which the goods are tendered accept the goods to be so carried under an agreement in risk note form "C" signed by the sender which exempt the Railway from all liability, however caused, even though no reduced rate is charged by the railway in this case. But the Railway is exempted from liability only if the loss occurs during transit. If any loss occurs after the transit has terminated and the goods have reached their destination, the Railway will be liable as a bailee if the loss is occasioned by its negligence or misconduct — that of its servants. The form of Risk Note C is given

<sup>1</sup> Ibid:—

<sup>2</sup> Ibid, S.

<sup>3</sup> Ibid, S. 73.

### RISK NOTE FORM C.

[Approved by the Governor-General in Council under section 72 (2) (b) of the Indian Railways Act, IX of 1890]

(To be used when, at sender's request, open wagons, carts or boats are used for the conveyance of goods liable to damage, when so carried, and which, under other circumstances, would be carried in covered wagons, carts or boats)

STATION.  
193 .

Whereas the consignment of \_\_\_\_\_ tendered by \_\_\_\_\_ as per Forwarding Order No \_\_\_\_\_ of \_\_\_\_\_ (date) for despatch by the Railway Administration or their transport agents or carriers to station under Railway Receipts No \_\_\_\_\_ of my (date), is at \_\_\_\_\_ request loaded in open wagons, carts or boats, to be our

so carried to destination, — the undersigned do hereby agree and undertake to hold the said Railway Administration and all other Railway Administrations working in connection therewith, and also all other transport agents or carriers employed by them respectively, over whose Railways or by or through whose transport agency or agencies the said goods may be carried in transit from station to station harmless and free from all responsibility for any destruction or deterioration of, or damage to the said consignment which may arise by reason of the consignment being conveyed in open wagons, carts or boats during transit over the said Railway or other Railway, working in connection therewith or during transit by any other transport agent or agencies employed by them respectively

WRITER (Residence) (Signature) WRITER. (Signature) (Residence)	Signature of sender Rank or { Father's name Grade      Age [Redacted] son
---	--

### RISK NOTE "D"

When a sender consigns dangerous, explosive or combustible articles at a "special reduced" or 'owner's risk' rate instead of an alternative "ordinary" or "risk acceptance" rate quoted in the tariff, the Railway Administration to which the goods are tendered accept, for the same for carriage under an agreement in risk note form which relieves the railway from all liability for any loss or damage excepting when such loss or damage is caused by the

of the railway or its servants. This risk note is very similar to risk note "B" in form. The form of risk Note D is given below :—

### RISK NOTE FORM D :

[Approved by the Governor General in Council under section 72 (2) (b) of the Indian Railways Act, IX of 1890]

(To be used when the sender elects to despatch at a "special reduced" or "owner's risk" rate, dangerous, explosive or combustible articles for which an alternative "ordinary" or "risk acceptance" rate is quoted in the Tariff)

STATION  
193

Whereas the consignment of

tendered by —  
us

as per Forwarding Order No \_\_\_\_\_ of \_\_\_\_\_ (date) for  
despatch by the Railway Administration to  
station, under Railway Receipt No \_\_\_\_\_ of \_\_\_\_\_ (date) is charged  
at a special reduced rate instead of at the ordinary tariff rate chargeable

I

for such consignments — the undersigned do in consideration of such  
we

lower charge, agree and undertake to hold the said Railway Administration harmless and free from all responsibility for any loss, destruction, deterioration of, or damage to the said consignment from any cause whatever, except upon proof that such loss, destruction, deterioration or damage arose from the misconduct of the Railway Administration's servants, provided that in the following cases —

(a) Non delivery of the whole of the said consignment or of the whole of one or more packages forming part of the said consignment packed in accordance with the rules and regulations for the time being in force for the packing of dangerous explosive or combustible articles, where such non delivery is not due to accident to train or to fire

(b) Pilferage from the package or packages forming part of the said consignment openly packed as in (a) when such pilferage is committed by the servants of the Railway Administration

the Railway \_\_\_\_\_ shall be bound to disclose to the consignor how the consignment was dealt with throughout the time it was in its possession or \_\_\_\_\_ and, if necessary to give evidence thereof before the consignor can call upon to prove misconduct, but, if misconduct on the part of the Railway Administration or its servants cannot be fairly inferred from such evidence the burden of proving such misconduct shall lie upon the consignor

I

— I further agree to accept responsibility for any consequences to the

<sup>1</sup> Railways

<sup>2</sup> Ibid, S. 75 of the aforesaid Railway Administration, or to the property of

<sup>3</sup> Ibid, S. 75 in that may be on the course of conveyance, which may be

caused by the explosion of, or otherwise by, the said consignment, and that all risk and responsibility whether to the Railway Administration, to their servants or to others, remain solely and entirely with —

*This agreement shall be deemed to be made separately with all Railway Administrations or transport agents or other persons who shall be carriers for any portion of the transit*

WITNESS (Signature)	Signature of sender Rank or	Father's name	
Residence	Caste	Age	
WITNESS (Signature) (Residence)	Profession Residence		

(To be filled up by Goods Clerk)  
Particulars of picking Date Goods Clerk

#### RISK NOTE "E" :

An agreement in risk note form E issued by the consigner is used by a Railway administration when booking elephants or horses of a declared value exceeding Rs 500/- a head, mules, camels or horned cattle Rs 50/- a head, donkeys, sheep, goats, dogs or other animals Rs 10/- a head, without the payment of the additional rate as authorised by S 73 of the Railways Act. When animals are booked under this risk note the Railway is liable only upto the amounts fixed by S 73 of the Railways Act, namely, Rs 500/- a head for elephants or horses, Rs 50 - 1 head for mules, camels, or horned cattle and Rs 10/- a head for donkeys, sheep, goats, dogs and other animals, provided any loss or damage is caused by its negligence or that of its servants. The form of Risk Note E is given below —

#### RISK NOTE FORM E:

[Approved by the Governor General in Council under section 72 (2) (b) of the Indian Railways Act, IX of 1890.]

To be used when booking elephants or horses of a declared value exceeding Rs 500 a head, mules, camels or horned cattle Rs 50 a head, donkeys, sheep, goats, dogs or other animals Rs 10 a head, without payment of the percentage on value authorised in section 73 of Act IX of 1890, as amended by section 4 of Act IX of 1896)

STATION.

193 . , I

compl

Whereas — the undersigned, have tendered to  
we

the work

Administration for despatch to station the animal (s) mentioned below, for which — have received Railway ticket No of this date.

And whereas — have paid to the said Railway Administration only we

their ordinary freight charge without any extra charge for insurance,

And whereas the said Railway Administration for such ordinary freight charges holds itself responsible for proved damages to (*each of*) the said animal (s) caused by neglect or misconduct of its servants to the extent of the value mentioned below,

And whereas the said Railway Administration has notified that it will not be liable for damage or loss arising from fright or restlessness, or delay not caused by the negligence or misconduct of its servants and such

condition is accepted by —

us

I —, the undersigned do in consideration of the foregoing terms and conditions hereby agree and undertake that the responsibility of the said Railway Administration and all other Railway Administrations working in connection therewith, and also all other transport agents or carriers employed by them respectively, over whose Railways or by or through whose transport agency or agencies the said animal (s) may be carried in transit from station to station, for the loss, destruction or deterioration of or damage to, (*each of*) the said animal (s) shall not exceed the value mentioned below —

No.	Description	Value of each	Animals		Value of each
			No.	Description	
	Elephant	500		Donkeys	10
	Horses	500		Sheep	10
	Mules	50		Goats	10
	Camels	50		Dogs	10
	Horned cattle	50		Other animals	10

WITNESS  
(Signature)

(Residence)  
WITNESS.

—. (Signature)  
(Residence)

Signature of sender  
Rank or { Father's name

Caste Age

Profession

Residence

<sup>1</sup> Rule.—The words *in instalments* should be scored out by the booking clerk.

<sup>2</sup> Ibid, S. 75.

<sup>3</sup> Ibid, S. 75 one animal is sent.

RISK NOTE "F":

When horses, mules and ponies are tendered for despatch in cattle truck or horse wagons instead of in horse boxes, the practice of a Railway Administration is to book them subject to an agreement in risk note Form "F" signed by the consignor which exempt the Railway from all liability in excess of Rs. 50/- per head for any loss, destruction or deterioration of or damage to any such animal despatched under the note. But the Railway will not be liable even to pay for this limited liability unless the loss or damage is caused by negligence or misconduct or that of its servants. The reason for this limitation of liability is that the rate for carriage in cattle truck or horse wagons is lower than the horse-box rate. The form of Risk note F is given below :—

**RISK NOTE FORM F :**

[Approved by the Governor-General in Council under section 72 (2) (b)  
of the Indian Railways Act, IX of 1890.]

(To be used when booking horses, mules and ponies, tendered for despatch in cattle-truck or horse-wagons instead of in horse-boxes).

STATION.

193

Whereas the consignment of  
me  
tendered by —, as per Forwarding Order No of  
us  
(date), for despatch by the Railway Administration to  
station, under Railway Receipt No of  
my me  
(date), at —, request and in consideration of the payment by — of  
our us  
cattle-truck or horse-wagon rate in lieu of horse-box rate, loaded in cattle-  
trucks or horse-wagons instead of horse-boxes to be so carried to destination ;  
And whereas the said Railway Administration has notified that it will  
not be liable for damage or loss arising from fright or restiveness, or delay  
not caused by the negligence or misconduct of its servants, and such con-  
dition is accepted by — :  
me

1

\_\_\_\_\_, the undersigned, do hereby agree and undertake to hold the said

Railway Administration and all other Railway Administrations working in connection therewith, over whose Railways the said animal(s) may be carried in transit from . . . station to . . . hermless and free from all responsibility in excess of Rs. 50/- (per head) for any loss, destruction or deterioration of, or damage to, the said animal(s) during transit over the said Railway or other Railways working in connection therewith.

Witness (Signature)	Rank or (Residence)	Signature of sender Father's name		
		Caste	Age	Profession
Witness (Signature)		Residence		
(Residence)				

RISK NOTE "G" i

Risk note "G" is used as an alternative to Risk Note "D," when the sender desires to enter into a general agreement for a series of consignments instead of executing a separate Risk Note for each consignment. It is Risk Note "D" with slight alterations in the language so as to make it applicable to more than one consignment.

**RISK NOTE "H":**

Risk Note 'H' is used in alternative to Risk Note 'B,' when the sender desires to enter into a general agreement for a series of consignments instead of executing a separate risk note for each consignment. It is in fact Risk Note 'A' with only such alterations as are necessary to make it applicable to more than one consignment.

**RISK NOTE "X":**

We have already seen that a Railway Administration is not liable for any loss of or damage to any article mentioned in the second schedule to the Railways Act, 1920, exceeding Rs 100 in value unless the consignor declares the value and contents of any consignment containing such an article and pays or undertakes to pay the additional rate, if required by the Railway Administration<sup>1</sup>. Where the consignor declares the value and contents of such a consignment but does not pay or agree to pay the additional rate, the Railway accepts the consignment for carriage under an agreement in risk note Form "X," which relieves the Railway of all liability for any loss of or damage to the consignment, howsoever caused. The Railway need not take such a risk note, for even in the absence of a risk note, the Railway will not be liable for any loss or damage. But the Railway insists

3 May

<sup>2</sup> Ibid., S. "ays Act, 1890, S. 75.

on it as a matter of practice. The form of risk Note "X" is given below :—

**RISK NOTE FORM X:**

(Approved by the Governor-General in Council Under Section  
72(2) (b) of the Indian Railways Act, IX of 1890).

(To be used when the sender elects to despatch an "excepted" article or articles specified in the second schedule to the Indian Railways Act, IX of 1890, whose value exceeds one hundred rupees, without payment of the percentage on value authorised in section 75 of that Act).

**Station  
194**

WHEREAS the Consignment of . . . tendered by ————— as per

forwarding Order No. .... (date) for despatch by the. .... Administration or their transport agents or carriers to .... Station, under Railway Receipt No. .... of. .... (date), is charged at the ordinary rates for carriage, and whereas I/we, have been required to pay, and elected not to pay, a percentage on the value of the consignment by way of compensation for increased risk. I/we, the undersigned do therefore agree and undertake to hold the said Railway Administration and all other Railway Administrations working in connection therewith, and also all other transport agents or carriers employed by them respectively over whose Railways or by or through whose transport agency or agencies the said goods may be carried in transit from. .... Station to. ....

Station harmless and free from all responsibility for any loss, destruction, or deterioration of, or damage to, the said consignment from any cause whatever before, during and after transit over the said Railway, or other Railway lines working in connection therewith or by any other transport agency or agencies employed by them respectively for the carriage of the whole or any part of the said consignment.

Rank or { Caste ... Age ...

**WITNESS:**

## **RISK NOTE "Y":**

Risk Note "Y" is used as an alternative to Risk Note "X," when the sender elects to enter into a general agreement for a term not exceeding six months for despatch of series of consignments containing excepted articles specified in the second.

to the Railways Act, 1890, exceeding Rs. 100/- in value without payment of the additional rate, instead of executing a separate risk note for each consignment. The form of Risk Note "Y" is the same as that of Risk Note "X" except certain minor alterations in the language in order to make it applicable to more than one consignment.

### SUITS :

#### *Notice under S. 77 of the Railways Act :—*

No suit against a Railway Administration for the loss, destruction, or deterioration of animals or goods or for refund of overcharges in respect of animals or goods carried by the Railway can be instituted unless a previous notice in writing of such claim is given to the Railway Under S. 77 of the Indian Railways Act, 1890, within six months from the date of the delivery of the animals or goods for carriage.

*Persons entitled to sue :—* The person who can sue a Railway for any loss of or damage to goods or animals delivered to the Railway, is the person in whom the property in the goods or animals is vested. As Baron Parke puts it, "the person whose property the goods are *prima facie* the party with whom the contract is made<sup>1</sup>." Thus where the property in the goods still remains vested in the consignor after their delivery to the carrier, as where a vendor consigns the goods to the buyer reserving the right of disposal<sup>2</sup>, the consignor is the only person who can sue. But where goods are delivered to a Railway by the seller for conveyance to the buyer and the receipt is made over to the buyer, the buyer alone, who is the consignee, can sue for any loss of or damage to the goods<sup>3</sup>. Similarly any person to whom the consignor has endorsed the railway receipt can institute a suit against the Railway for any loss or damage as he becomes entitled to the goods by virtue of such endorsement<sup>4</sup>.

#### *Notice under S. 80 of the Civil Procedure Code :—*

Where a Railway is a state Railway i.e., administered by the

<sup>1</sup> *Mullinson vs. Carver* (1843) 1 L. T. (O. S.) 59;

<sup>2</sup> See *Sale of Goods Act, Supra*.

<sup>3</sup> *M. & S. M. Ry. Co. Ltd. vs. Ringawami Chetti.*, A. I. R. (1924)

<sup>2</sup> *Ibid.* Mad. 517

<sup>3</sup> *Ibid.* *Bire Lal Gopi vs. E. I. Ry. Co.*, 46 All. 691.

Government of India, any suit against the Railway must be brought against the Governor-General in Council after serving a notice under S 80 of the Civil Procedure Code, specifying the cause of action the names and addresses of the parties to the suit, and the relief claimed at least two months prior to the institution of the suit besides serving a notice to the Railway under S 77 of the Railways Act. In default of serving a notice under S 80 of the Civil Procedure Code, the suit must fail.

*Lawsuit* —The period of limitation is the same as in the case of a suit against a common carrier.

#### Carriage by sea :

*Contract of affreightment* A shipper who wants to ship goods by sea has to enter into a contract with a ship-owner unless he possesses a ship himself. When a ship owner agrees to carry goods by water or to furnish a ship for the purpose of so carrying goods, in return for a sum of money to be paid to him such a contract is called a *contract of affreightment*, and the sum to be paid is called *freight*.<sup>1</sup> A contract of affreightment may be (a) either contained in a document called a charter party or (b) evidenced by a document called a *bill of lading*.

#### Charterparty :

When a ship owner agrees to carry a complete cargo of goods for a shipper or to furnish a ship for that purpose the *contract of affreightment* is almost always set out in a formal document called a *charterparty* which contains the terms and conditions under which the goods are shipped. A charterparty may either take the form of a lease or demise of the ship by the ship owner to the shipper for the purpose of carrying the goods the shipper hiring the ship for such purpose or contain an undertaking by the ship owner to carry the goods the shipper undertaking to provide a full cargo. The shipper under a charterparty contract is called the charterer.

Where a charterparty contract takes the form of a demise or lease of the ship to the charterer, the charterer becomes for the

<sup>1</sup> Scruton on Charterparties and Bills of Lading, 12th ed. 2.

time being the owner of the vessel and the master and the crew become for all purposes his servants and through them the possession of the ship becomes vested in the charterer. A charterer by way of demise has, therefore, all the rights and is subject to all the liabilities of a shipowner. But where the charterparty is not by way of a demise, all that the charterer acquires is the right to use the ship for loading and carrying his goods and the ownership and the possession of the ship remains in the shipowner and the master and the crew continue to be the employees of the ship-owner. It is difficult to determine whether a charterparty is by way of a demise or an ordinary one and the tendency of courts in recent times has been against construing a charter as a demise or lease.<sup>1</sup> The true test seems to be as observed by Lord Esher in *Bumvall v. Gilchrist & Co.*<sup>2</sup> whether the owner has for the time parted with "the whole possession and control of the ship." Thus where a charter stipulated that the ship was "to be let for the sole use of charterers and for their benefit for six months

the owners supplying all ship's stores, and paying crew's wages . . ." it was held that the charter was not a demise even though it uses the words "to be let etc." as the ship-owner did not part with the whole possession and control of the ship, having reserved the right to pay crew's wages<sup>3</sup>. But where a ship-owner purchased the ship for the purpose of selling it to the charterer on the terms that part of the purchase money would be paid at once and the balance on the expiration of the charter and where the charterparty provided that the ship was to be let to the charterer for four months, the charterer paying the wages of the captain and the crew it was held that the shipowner had parted with the possession and control of the ship and the charter was by way of a demise<sup>4</sup>.

A charterer may himself ship the cargo or enter into sub-contracts with separate shippers, who may ship cargo by the chartered ship under separate bills of lading.

<sup>1</sup> Scrutton on Charterparties and Bills of Lading, 12th ed. p. 5 ; per Vaughan Williams, L.J., in *Herne Bay Co. v. Hutton*, (1903) 2 K.B. at p. 689.

<sup>2</sup> (1892) 1 Q. B. 253; (1893) A. C. 8.

<sup>3</sup> *Imca Coal & Iron Co. v. Huntley* (1877), 2 C. P. D. 464.

<sup>4</sup> *Ibid.* ~~v. Gilchrist & Co.~~, (1893) A.C. 8.

**Effect of a charterparty by way of demise :**

It has already been noted that a charterer by way of demise has all the rights and is subject to all the liabilities of a shipowner and he is to be regarded as the owner of the ship *pro tempore* (*i.e.*, for the time being) during the continuance of the charter. The effects of such a charterparty may be enumerated as follows<sup>1</sup>:—

- (a) The shipowner, being out of possession, would have no lien at common law on the goods shipped for the freight due thereon under the charter.
- (b) The shipowner, having ceased to be the owner, would not be liable to the shippers who ship goods through the charterer for any loss or damage to the goods or for any acts of the master or the crew even if they did not know of the charter<sup>2</sup>.
- (c) The master would be the agent of the charterer and delivery to him of goods bought by the charterer would deprive the unpaid seller of his right of *stoppage in transit* unless the bill of lading was made deliverable to the shipper or his order. Where the charter is not a demise, delivery to the master would be delivery to a carrier and the right of stoppage in transit would remain<sup>3</sup>.
- (d) A charterer by a demise would be regarded as a carrier within the meaning of the Carriage of Goods by Sea Act, 1925, and would be entitled to all the protection given there to a shipowner.<sup>4</sup>
- (e) A charterer by a demise would be entitled to the benefits conferred on an owner by Secs. 502 and 503 of the Merchant Shipping Act, 1894.

**Bills of Lading :**

When the master or the owner of a ship has agreed with separate shippers to convey goods to the place of her destination, the ship is called a *general ship*. The contract of affreightment

<sup>1</sup> Scrutton on Charterparties and Bills of Lading, 12th ed., p. 6.

<sup>2</sup> Baumvoll *v.s.* Gilchrist & Co. (1893) A.C. 8.

<sup>3</sup> See the cases discussed on this point in the Chapter on Sale of C

<sup>4</sup> Art. I (a) of the Schedule XX.

as to each parcel of goods shipped in a general ship may be contained in a charterparty but is more usually evidenced by a document called a *bill of lading*<sup>1</sup>. "A bill of lading is in every case a receipt for goods shipped on board a ship, signed by the person who contracts to carry them, or his agent, and stating the terms on which the goods were delivered to and received by the ship"<sup>2</sup>. A bill of lading, unlike a charterparty, is not the contract but only an excellent evidence of the terms of the contract<sup>3</sup>.

### The issue of Bill of Lading :

The contract of affreightment in the case of a bill of lading is usually concluded before the bill of lading is issued. The contract is concluded and the bill of lading is issued in the following manner. The voyage is first advertised, usually by means of shipping cards. Then prospective shippers book different spaces on the ship for their goods by means of a *freight engagement notes*. In most cases there is a concluded agreement between a shipper and the owner as soon as the shipper books a space, the shipper being deemed to have agreed to ship his goods and the shipowner being regarded as having agreed to carry the same on the terms of his usual bill of lading<sup>4</sup>. The shipper then delivers his goods to those who are in charge of the ship and is given in exchange a *mate's receipt* signed by one of the ship's officers or the ship's agent which shows that the goods have been delivered to the ship. The shipper then usually preserves three forms of bills of lading appropriate to the transaction and fills them up with the necessary details. These forms along with the mate's receipt are then taken to the shipowner who signs them and returns one of the signed bills of lading to the shipper, retaining the other two signed bills of lading and the mate's receipt for himself.

### Form of Bill of Lading :

"The usual form of bill of lading is the '*shipped*' bill of lading, so called because it usually commences with the words

<sup>1</sup> Scrutton on Charterparties and Bills of Lading, 12th ed. p. 2.

<sup>2</sup> *Ibid.*, p. 9.

<sup>3</sup> Per Lord Bramwell in *Sewell v. Burdick* (1884), 10 A. C. 105.

<sup>4</sup> H. Smith's Mercantile Law, 13th ed., p. 362; *De Clermont v. General*

<sup>5</sup> *Ibid.*, N. Co. (1891) 7 T. L. R. 187.

'shipped in apparent good order and condition' or words to the like effect, and acknowledges the actual receipt of the goods on board a named ship<sup>1</sup>."

But there is another form of bill of lading which simply acknowledges that goods have been received by the shipowner for shipment and does not admit whether the goods have been put on board a ship or not. These bills of lading are known as "*received for shipment*" bill of lading. Where the bill of lading is issued in India, the carrier, whether the ship-owner or the charter as the case may be, must under S. 7 of the Carriage of Goods by Sea Act, 1925, issue a 'shipped' bill of lading if the shipper so demands. But if the shipper has previously taken a "received for shipment" bill of lading or a similar document of title he must surrender it when he takes a 'shipped' bill of lading. The carrier may, however, at his option note the fact of shipment and the name or names of the ship or ships upon which the goods have been shipped on a bill of lading already issued instead of issuing a fresh "shipped" bill of lading and on such noting the bill of lading already issued will be deemed a 'shipped' bill of lading.

A bill of lading usually contains a statement as to the condition of the goods and a bill of lading issued in India must state the apparent order and condition of the goods<sup>2</sup>. The carrier cannot evade this obligation in India by stating "weight, quality and quantity unknown." Where a bill of lading states that the goods have been shipped in "good order and condition," it will amount to an admission that the goods were in good order and condition at the time of shipment so far as could have been judged by the exterior of the goods.

#### Requirements under the Carriage of Goods by Sea Act :

Under the carriage of Goods by Sea Act, 1925, a bill of lading including a similar document of title issued in respect of cargo shipped from an Indian port must contain the following:—

- (a) It must contain a clause paramount, i.e., a statement

<sup>1</sup> Smith's Mercantile Law, 13th ed., p. 332.

<sup>2</sup> Article III, r. 3 (c) of the Schedule to the Carriage of Goods by Act, 1925.

that it is to have effect subject to the rules laid down in the Act<sup>1</sup>.

- (b) It must contain statements showing among others (i) the leading marks necessary for identification of the goods as the same are furnished in writing by the shipper before the loading of such goods starts, provided such marks are stamped or otherwise shown clearly upon the goods if uncovered, or in the cases of coverings in which such goods are contained, in such a manner as should ordinarily remain legible until the end of the voyage; (ii) the number of packages or pieces or the quantity or weight, as the case may be, as furnished in writing by the shipper; and (iii) the apparent order and condition of the goods; provided that no carrier, master or agent of the carrier, should be bound to state or show in the bill of lading any marks, number, quantity or weight which has reasonable grounds for suspecting not accurately to represent the goods actually received, or which he has had no reasonable means of checking<sup>2</sup>.

#### **Effects of a Bill of Lading :**

The effects of a bill of lading issued under a charterparty are as follows :—

1. A bill of lading is binding on the shipowner if signed by the master within the ordinary scope of his authority even if the ship is chartered unless the charter amounts to a demise, or the shipper knew of the existence of the charter at the time of shipment and the shipper can sue the owner if the goods are lost or damaged by any cause not excepted in the bill of lading. In *Sandeman v. Sewer*<sup>3</sup>, A, the shipowner chartered a ship to C, the charterer, to sail to X, and load from C's agent there. The charterparty provided that the master should sign bills of lading without prejudice to the charter (i.e., without conflicting with any provision of the charter). At X goods were shipped by shippers who knew nothing of the charter, under a bill of lading signed by the master. It was held that the shippers could sue A,

<sup>1</sup> Carriage of Goods by Sea Act, 1923, S. 4.

<sup>2</sup> *Ibid.*, r. 3, Art. III of the Schedule.

<sup>3</sup> *Ibid.*, 1886, L.R. 2 Q.B. 86.

the master having signed as his agent. Similarly the shipowner will not be able to rely on any restriction on the authority of the master to sign a bill of lading in a particular form imposed under a charterparty which otherwise would be within the ordinary authority of the master unless the shipper knew of the terms of the charter<sup>1</sup>.

2. Where a bill of lading is issued to a shipper, other than the charterer, who ships goods on a ship which is chartered by way of a demise, the charterer alone is liable for any loss or damage to the goods covered by the bill of lading whether the shipper knew of the charter or not<sup>2</sup>.

3. Where a shipper has notice that the ship is chartered and that under the charter the master is the agent of the charterer in signing bills of lading, the shipper can sue the charterer only for any loss or damage even if the charter does not amount to a demise. In *Saphuel v. West Hartlepool Steam Navigation Co.*<sup>3</sup> a shipper shipped oil in a chartered ship under a bill of lading, the contract providing that the charterer's form of bill of lading was to be used. The bill of lading was in fact signed by the master on the charterer's form. It was held that the shipper could not sue the shipowner as his contract was with the charterer. But it was held in *Manchester Trust v. Furness, Willy & Co.*<sup>4</sup> that a mere reference of a charterparty in a bill of lading by inserting a clause like "all other conditions as per charter" does not fix the shipper with knowledge that the master was signing the bill of lading as the agent of the charter unless it is expressly stated in the bill of lading or a copy of the charter is annexed to the bill of lading<sup>5</sup>.

4. Where the charterer is himself the shipper, the bill of lading is to be regarded as merely a receipt for the goods and cannot vary the terms of the charter unless the parties expressly and clearly intend to effect such variation. As Lord Bramwell observed in *Wagstaff v. Anderson*<sup>6</sup>, "to say that the bill of lading is a contract, superseding, adding to, or varying the former con-

<sup>1</sup> Scrutton on Charterparties and Bills of Lading—12th Ed., 59.

<sup>2</sup> *Beumvoll v. Gilchrist*, (1893) A.C. 8.

<sup>3</sup> (1906), 11 Com. Cas. 115.

<sup>4</sup> (1895) 2 Q.B. 539 (C.A.)

<sup>5</sup> *The Draupner* (1910) A.C. 450.

<sup>6</sup> (1880), 5 C.P.D. at p. 177.

tract, is a proposition to which I can never consent." If the holder of a bill of lading is an agent of the charterer the effect of the bill of lading would be the same<sup>1</sup>. In *Rodocanachi v. Milburn*<sup>2</sup> the master of a chartered ship was authorised, under the charter, to "sign bills of lading, at any rate of freight, and as customary at port of lading, without prejudice to the stipulations of the charter." The charterer shipped goods under the charter and the master signed a bill of lading containing a stipulation that the shipowners would not be liable for "the negligence of the master and the crew" which was not in the charter. The goods were lost through the negligence of the master. It was held that the master could not insert a clause in the bill of lading ~~of the~~ to the prejudice of the charter and the bill of lading was ~~merely~~ except and the shipowners were liable.

5. Where a bill of lading, issued to a charterer who is also the shipper, is transferred to a nonafide transferee for value without notice of the terms of the charterparty the shipowner cannot rely on the charterparty as against such transferee and is bound by the terms of the bill of lading. The position would be the same as against a shipper or an endorsee from him who takes a bill of lading in ignorance of the terms of a charterparty.<sup>3</sup> In the *Patria*<sup>4</sup> a ship was chartered to C under a charterparty which relieved the shipowner of liability for certain excepted perils including "restraint of princes." F shipped goods to G in ignorance of the charter and the master signed a bill of lading containing only an exception of "perils of the Sea". The goods were lost for "restraint of princes." In an action by G, who was also ignorant of the charter, against the shipowner, it was held that the shipowner was liable as the bill of lading did not contain an exception of "restraint of princes" and that the bill of lading was not affected by the terms of the charter of which both F and G were ignorant.

The effects of a bill of lading whether issued under a charter-party or not are as follows :—

1. A bill of lading signed by the master within the terms of his authority is *prima facie* evidence against the carrier (*i.e.*,

<sup>1</sup> *San Roman* (1872), L.R. 3 A. & E. 583, 592.

<sup>2</sup> *Ibid.* 1886, 18 Q.B.D. 67.

<sup>3</sup> *Ibid.*, <sup>4</sup> L.R. 3 A. & E. 436.

## LAW RELATING TO CARRIAGE OF GOODS

the shipowner or the charterer, where the charter is a demise or the bill of lading is signed by the master as the agent of the charterer to the knowledge of the shipper) that the quantity or weight of the goods stated therein has been delivered on the ship<sup>1</sup>. If the carrier cannot deliver the full quantity he will be liable for any deficiency unless he can prove that the quantity stated in the bill is incorrect<sup>2</sup>. Under the Carriage of Goods by Sea Act, 1925<sup>3</sup>, a bill of lading must show the number of packages or pieces or the quantity or the weight and the apparent order and condition of the goods which are *prima facie* evidence against the carrier. The carrier will be liable for any deficiency in the weight or quantity of packages and of the goods as stated unless he can state in the bill of lading relat-

Lading  
for  
the transferee  
are conclusive  
statements as to their quality, quantity or  
correct and the carrier will be liable to the transferee  
every or deficiency in the quality or quantity or weight  
goods as stated in the bill of lading<sup>4</sup>. But the carrier will  
be liable even to a transferee for value if the bill was obtained  
by representation or fraud of the holder of the bill or the  
shipper or some person under whom the holder claims or if the  
holder knew at the time of the transfer of the bill to him that the  
statements in the bill were incorrect<sup>5</sup>.

3 In the case of a bill of lading issued in India, the shipper is deemed to guarantee the accuracy of the statements, furnished by him e.g., as regards the quality or quantity of the goods and incorporated in a bill of lading and is bound to indemnify the carrier for any loss, damage or expenses arising from any inaccuracy in such statement e.g., when the carrier becomes liable to a bonafide transferee for value<sup>6</sup>.

4 Where any particular weight of a bulk cargo is accepted

<sup>1</sup> Carriage of Goods by Sea Act, 1925, r. 4 Art. III of the Schedule.

<sup>2</sup> Smith *vs.* Bedouin S N Co (1896) A.C. 70

<sup>3</sup> R. 2, Art. III of the Schedule.

<sup>4</sup> Brown *vs.* Powell Coal Co (1873), L.R. 10 C.P. 562

<sup>5</sup> Valieri *vs.* Royland (1866) L.R. 1 C.P. 382.

<sup>6</sup> Carriage of Goods by Sea Act, 1925, r. 5, Art. III of the Schedule.

by a third party other than the carrier and is incorporated as such in a bill of lading issued in India, such weight as stated in the bill of lading will not be *prima facie* evidence against the carrier and the shipper will not also be deemed to guarantee the accuracy thereof and the carrier will not be liable for any deficiency in the weight even to a transferee of the bill of lading for value.

#### **Bill of Lading a document of title-functions :**

A bill of lading has been defined as a document of title in the Sale of Goods Act<sup>1</sup>. Its function is twofold, namely, (a) it serves as an evidence of the contract between the shipper and the carrier and ~~it serves as a symbol of the goods shipped~~. In the latter case it is a document of title in the sense that at ~~it is regarded as a symbolic transfer of the goods to the transferee as it was between the parties~~ The transferor may intend to transfer absolute ownership in the goods or (b) ~~to impose the property conditions~~ acceptance of bills of exchange for the price or (c) to ~~to give~~ gage of the goods as security for an advance or (d) ~~to~~ pledge of the goods for the same purpose or (e) to pass no property at all in the goods as when no consideration is paid for the trans

The function of a bill of lading as a document of title is ~~evidently~~ summarised by Bowen I. J. in *Sanders vs. Maclean*<sup>2</sup> in the following words :—

"A cargo at sea, while at the hands of the carrier, is generally incapable of physical delivery. During this period of transit and voyage, the bill of lading by the law merchant is universally recognised as its symbol ; and the indorsement and delivery of the bill of lading operates as a symbolic delivery of the cargo. Property in the goods passes by such indorsement and delivery of the bill of lading, whenever it is the intention of the parties, that the property should pass, just as under similar circumstances the property would pass by an actual delivery of the goods. And for the purpose of passing such property in the goods and completing the title of the

<sup>1</sup> S. 2 (4).

<sup>2</sup> *Sewell vs. Burdick* (1884), 10 A.C. 74.

<sup>3</sup> *Scruton on Charterparties and Bills of Lading*, 12th Ed. pp. 190, 191.

<sup>4</sup> *Ibid.* (1883), 11 Q.B.D. 327 at p. 341.

indorsee to full possession thereof, the bill of lading, until complete delivery of the cargo has been made on shore to someone rightfully claiming under it, remains in force as a symbol and carries with it not only the full ownership of the goods, but also all rights created by the contract of carriage between the shipper and the shipowner.<sup>1</sup> It is a key which, in the hands of a rightful owner, is intended to unlock the door of the warehouse, floating or fixed, in which the goods may chance to be.

#### Transfer of Bill of Lading :

A bill of lading making goods deliverable "to order" or "to order or assigns" of the consignee or "to order" or "to order or assigns" of a blank name is by mercantile custom negotiable by indorsement and delivery and ~~and delivery~~ making goods deliverable to bearer is similarly negotiable by mere delivery.<sup>2</sup> But a bill of lading, which makes goods deliverable to a specified person and does not show on the face of it that it is transferable eg where it does not show that the goods are deliverable to the "order or assigns" of the consignee or of a blank name, is not negotiable.<sup>3</sup> Indorsement may be effected by the shipper on the consignee writing his name on the back of the bill. The indorsement may be "in full" or special i.e., in favour of a specified person in which case the indorsee transfers it again only by indorsing it.<sup>4</sup> The indorsement may, however, be "in blank" in which case the bill of lading may be transferred again by mere delivery.<sup>5</sup>

#### Bills of Lading if Negotiable Instruments :

Although a bill of lading, which makes goods deliverable to "order" or "to order or assigns" of a named person or a name left blank or "to bearer", is negotiable by indorsement and delivery or delivery only as the case may be, and property in the goods may pass if that was the intention of the parties to the transfer, yet such a bill of lading cannot be regarded as a negotiable instrument.

<sup>1</sup> Bills of Lading Act, 1855, S. 1.

<sup>2</sup> Scrutton on Charterparty and Bills of Lading, 12th Ed. p. 187

<sup>3</sup> Henderson *vs.* Comptoir d' Ecompte de Paris (1873), 4 L. R. 5 p.c. 253 at 259.

<sup>4</sup> Lickbarrow *vs.* Mason (1794), 5 T.R. 683.

<sup>5</sup> Per Lord Selborne in Sewell *vs.* Burdick (1884), 10 A.C. 74 at 7

The characteristic feature of a negotiable instrument is that a holder in due course acquires a valid title to the instrument, even as against the true owner, irrespective of any defect in the title of his transferor in all cases excepting when he derives his title through a forged indorsement<sup>1</sup>. But the holder of a bill of lading takes the bill subject to any defect in the title of his transferor or any person from whom his transferor derives his title whether he is a holder for value without notice of such defects or not. The difference between a negotiable instrument and a bill of lading is, therefore, that in the former case a holder in due course takes a better title than his transferor, where in the latter case the holder takes only such title as his transferor possesses. Thus where A ships goods to C and sends the bill of lading to C along with a bill of exchange for the price on the condition that C can take the bill of lading on accepting the bill of exchange, the intention of the parties is that the property in the goods will only pass on C's acceptance of the bill of exchange<sup>2</sup>. If C takes the bill of lading wrongfully without accepting the bill of exchange and indorses it in favour of D who takes it bona fide and for value, D will have no title to the goods as against A though he was not aware of the defect in C's title. A bill of lading is, therefore, negotiable only in a popular sense and not in a technical sense<sup>3</sup>.

But in the following cases a bona fide transferee for value with out notice acquires a better title than his transferor even in the case of a bill of lading —

(a) Where an unpuid vendor has parted with the property in the goods absolutely and has handed over the bill of lading to the consignee, a bona fide indorsee for value from the consignee of the bill of lading would take the goods free of the right of the vendor to stop the goods in transit<sup>4</sup>.

(b) Where a bill of lading issued under a charterparty by the shipowner to the shipper whether the charterer or not, differs in its terms from the charter, the shipper

<sup>1</sup> S 58 of the Negotiable Instruments Act, also see the chapter on Negotiable Instruments

<sup>2</sup> Currie vs Behrend (1854), 3 E & B at pp 633, 634

<sup>3</sup> Sale of Goods Act, S 25.

<sup>4</sup> Scruton on Charterparties and Bills of Lading, 12th ed p 188

<sup>5</sup> Ibid, 210

if he is the charterer or is aware of the charter; is bound by the terms of the charter. But if the bill of lading is transferred by the charterer or the shipper, who is aware of the charter, to a<sup>1</sup> bonafide holder for value who takes it ignorant of the terms of the charter, such transferee will take the bill unaffected by the terms of the charter even though the agent of the shipowner who signed the bill of lading had no authority to sign it provided it was within the ordinary authority of the agent and the difference in the terms of the bill of lading was not obtained by fraud of any previous holder<sup>2</sup>. Thus if any clause contained in the charterparty limiting the liability of the shipowner is not incorporated in the bill of lading, a bonafide indorsee for value of the bill of lading would take it free from the operation of such clause limiting the liability and can sue the shipowner for any loss or damage which is not excepted in the bill of lading though it might have been so in the charter-party.

- (c) Where a mercantile agent is, *with the consent of the owner*, in possession of the bill of lading in respect of the shipment of those goods, an indorsee or transferee for value of the bill of lading from him whether by way of sale, mortgage or pledge would acquire a valid title of the goods as against the true owner, provided the indorsee or transferee acts in good faith and has not noticed that the agent has no right to transfer the bill of lading.
- (d) Where a person, having sold goods, continues in possession of the bill of lading in respect of the goods, a transfer of the bill of lading by him or his mercantile agent whether by sale, mortgage or pledge, would confer a valid title in respect of the goods to any transferee for value who takes the bill in good faith and without notice of the previous sale.<sup>3</sup>

<sup>1</sup> Mitchell *vs* Scaife (1815), 4 Camp. 298.

<sup>2</sup> The Patria (1871) L.R. 3 A & E. 436; Chappel *vs* Comfort (1861), 10 C. B. N. S. 802; Manchester Trust *vs* Furness (1895) 2 Q. B. 539; Turner *vs* Haji Goolam (1904) A.C. 826.

<sup>3</sup> Sale of Goods Act, S. 27; Contract Act, S. 178.

<sup>4</sup> Sale of Goods Act, S. 30 (1);

(c) Where a person, having bought or agreed to buy goods, obtains, *with the consent of the seller*, possession of the bill of lading in respect of the goods before he becomes the owner of the goods, as when a purchaser under a hire purchase agreement obtains the bill of lading before any instalment of the price has been paid, a transfer of the bill of lading whether by way of sale, mortgage or pledge would pass a valid title to the transferee as against the original seller provided the transferee takes the bill for value and in good faith and without notice of any lien or other right of the original seller.<sup>1</sup>

#### **Warranties and Terms :**

A contract of affreightment, whether contained in a charter-party or evidenced by a bill of lading, contains statements, which are either of facts as then existing e.g., the then position or condition of the ship or are promises for the future e.g., that the ship will be ready to load by a given day. Statements as to promises for the future are usually to be found in a charterparty and are absent in a bill of lading ; for a bill of lading is issued after the goods have been shipped or delivered for being shipped whereas the process of shipping and loading in the case of a charterparty takes place after the signing of the charterparty. The statements in a contract of affreightment are either warranties or terms. A warranty in a maritime contract as in a marine insurance contract denotes a term which is usually called a "condition" and which is so essential to the contract that its non-fulfilment entitles the party relying thereon to repudiate the contract. "It is either an affirmation or promise of the existence of some fact or facts upon the non-existence of which the contract ceases to exist."<sup>2</sup> A term, on the other hand, means any affirmation or promise which is not so vital as to make the contract dependent upon its truth. It corresponds to a warranty in an ordinary contract and its breach only gives rise to a right for damages to the aggrieved party. Whether a term in contract of affreightment is a warranty or a term is to be determined by the court from the intention of the parties to be gathered from all the surrounding circumstances.<sup>3</sup> In Suger *vs.*

<sup>1</sup> *Ibid.*, S. 30 (2).

<sup>2</sup> *Commercial Laws of the World*, Vol. XIII, p. 520.

<sup>3</sup> *Ibid.* *vs. Burness* (1863), 3 R. & 751.

ber, or Charterers to have the option of cancelling the agreement. Duthie<sup>1</sup> a ship was chartered to be ready on or before 10th November. It was held that such readiness was a condition precedent or warranty, the breach of which would entitle the charterer to cancel the agreement. The same charter also contained a clause that the Captain should attend daily at the broker's office to sign bills of lading. It was held that such a daily attendance was only a term and not a warranty.

A party entitled to repudiate a contract of affreightment for breach of warranty may waive it and treat it as a mere term and sue for damages for its breach. In the case of a bill of lading disputes occur very rarely as to whether a term is a warranty or not because the shipper can hardly discover a breach of warranty before the ship has sailed and has no opportunity of taking his goods back and the shipper has to seek his remedy by way of damages in case of any breach of warranty.

Warranties may be either express or implied by law.

#### **Implied Warranties :**

The following warranties are implied in every contract of affreightment unless they are excluded by clear and unambiguous words<sup>2</sup>:

(1) *Warranty of Seaworthiness* :—A carrier by contracting to carry goods in a ship impliedly warrants that his ship is seaworthy for the purpose of the particular voyage,<sup>3</sup> that is, she is fit in all respects to carry her cargo safely to its destination, having regard to all the ordinary perils to which such a cargo would be exposed on such a voyage.<sup>4</sup> The seaworthiness must exist not only at the commencement of loading but also at the time of sailing from the port of loading.<sup>5</sup>

In *Cohen vs. Devidson*,<sup>6</sup> a ship was chartered to proceed to a

<sup>1</sup> (1860) 8 C.B.N.S. 45.

<sup>2</sup> *Rathbone vs. McIver*, (1903) 2 K.B. 378; *Elderslie vs. Borthwick*, (1905) A.C. 93; *Nelson vs. Nelson*, (1908) A.C. 16; *Chartered Bank vs. B.I.S.N. Co.*, (1909) A.C. at p. 375.

<sup>3</sup> *Steele vs. State Line Steamship Co.* (1877), 3 A.C. 72.

<sup>4</sup> *Hedley vs. Pinkney S. S. Co.*, (1894) A.C. at p. 227; *Maori King vs. Hughes* (1895) 2 Q.B. 550.

<sup>5</sup> *Scrutton on Charterparties*, 12th ed. p. 99.

<sup>6</sup> (1877) 2 Q.B.D. 455.

a wharf in a river and there take on board a cargo and sail for another port. It was found that the ship was seaworthy when she began to load but unseaworthy when she put to sea. It was held that the shipowner was guilty of breach of warranty for sailing to make the ship seaworthy at the time she put to sea after loading.

There is no fixed standard for determining seaworthiness. Seaworthiness is a relative term and varies according to the nature of the voyage and the cargo to be carried. Thus a ship may be seaworthy for a voyage in home waters but unseaworthy for a voyage across the Atlantic<sup>1</sup> or for a voyage at one season of the year and not for a voyage at another season. Similarly a ship carrying wheat may be seaworthy without a refrigerating machinery or one which is out of order but a ship carrying frozen meat must have a refrigerating machinery in order before it sails in order to be seaworthy. Thus in *Maori King vs. Hughes*,<sup>2</sup> where frozen meat carried by a ship was damaged by a breakdown of the refrigerating machinery due to a defect which existed when the voyage started, it was held that the warranty of seaworthiness was broken and the shipper was entitled to recover damage from the shipowner, though the bill of lading provided that "the steamer shall not be accountable for the condition of goods shipped under this bill of lading, nor for any loss or damage thereto arising from failure or breakdown of machinery". If, however, the defect due to which the machinery broke down arose after the voyage had started, the shipowner would not have been liable as the damage would have come under the exception. In this case the exception did not expressly limit the liability of the shipowner for unseaworthiness at the start and hence he was held liable. Similarly in *Stanton vs. Richardson*,<sup>3</sup> it was held that the charterer was entitled to cancel the charterparty where it was found that the chartered ship was seaworthy to carry any cargo except wet sugar which was the cargo to be carried under the charterparty and for which the ship had not pumps of sufficient capacity.

Where a voyage is to be performed in different stages, during which the ship requires different kinds of, or further, preparation or equipment, there is an implied warranty that at the commence-

<sup>1</sup> Smith's Mercantile Law, 13th ed. p. 340.

<sup>2</sup> (1895) Q.B. 550.

<sup>3</sup> *Ibid.* <sup>4</sup> (1875), L.R. 9 C.P. 390.

ment of each stage the ship is seaworthy in respect of her preparation or equipment for the purposes of that stage. Thus where a voyage includes a stay in a port of loading, sailing down a river to the open sea and then an open sea voyage, there are three stages in the voyage and at the commencement of each of the three stages she should be seaworthy for the purposes of that particular stage. Thus while sailing down the river, it will be enough for her to sail with a river crew and without the heavy equipment necessary for a sea voyage. But while taking to the sea she must have a seagoing crew and the heavy equipment necessary for a sea voyage in order to be seaworthy<sup>1</sup>.

Where the undertaking as to seaworthiness is broken and the shipper discovers it before the voyage begins he can treat the contract as repudiated by the shipowner and refuse to load his goods. But if he discovers the breach subsequently he can recover any loss sustained by him by reason of the unseaworthiness. Under the common law a shipowner is absolutely liable for any loss caused by unseaworthiness at the starting of the voyage even where the unseaworthiness would not be discovered with all the care and diligence unless he is expressly protected from such liability by exceptions in the charter or the bill of lading.<sup>2</sup> But under the Carriage of Goods by Sea Act, 1925,<sup>3</sup> the undertaking of the ship-owner is only to exercise due diligence to make the ship seaworthy where goods are shipped under a bill of lading whether under a charterparty or not. The shipowner is not, therefore, liable in cases of shipments under bills of lading issued in India for any unseaworthiness which could not be discovered by due diligence or care. But under the carriage of goods by Sea Act, 1925,<sup>4</sup> the shipowner cannot, by any express provision in a bill of lading, relieve himself of his liability for any loss caused by his neglect or default in exercising due diligence to make the ship seaworthy which he is still permitted to do under the common law where goods are shipped under a charterparty.<sup>1</sup>

(2) *Implied warranty of reasonable despatch* :—In every contract of affreightment the carrier impliedly undertakes that the

<sup>1</sup> *McFadden vs. Blue Star Line* (1905) 1 K. B. 697; *Wade vs. Cockerline* (1905), 10 Com Cas. 115; *Rid & Co. vs. Page, Son & East*, (1927) 1 K. B. 743.

<sup>2</sup> *Bank of Australia vs. Clan Line* (1916) 1 K. B. 39.

<sup>3</sup> Art. II, r. 1.

<sup>4</sup> Art. II, 48.

ship "shall be ready to commence the voyage agreed on, and to load the cargo to be carried, and shall proceed upon and complete the voyage agreed upon, with all reasonable dispatch".<sup>1</sup> A breach of this undertaking may amount to a repudiation of the contract or may give the shipper only the right to recover damages for any loss which he may have suffered due to delay.

Thus if by a breach of this undertaking there is such delay as goes to the root of the whole matter, and deprives the charterer or the shipper of the whole benefit of the contract or entirely frustrates the object of the charterer or the shipper in shipping the goods, the charterer or shipper may refuse to ship or load the goods.<sup>2</sup> But if the delay is not so serious as to discharge the contract, the charterer or the shipper cannot refuse to load, but the carrier will be liable for damages unless the delay is due to some cause for which the carrier is not liable under the excepted clause in the contract of affreightment. In *Mac Andrew vs. Chapple*,<sup>3</sup> a ship was chartered "with all convenient speed, having liberty to take an outward cargo for owner's benefit, direct on the way, to proceed to a named port, and there load a full cargo" The ship deviated to another port which was not "direct on the way" to the named port and arrived at the named port a few days late. The charterers, thereupon, refused to load. It was held that the charterer was not entitled to refuse to load as the object of the voyage was not frustrated, but could recover damages for the delay.

<sup>1</sup> In some cases the circumstances which cause the delay may render the performance of the contract impossible and bring about what is called in the language of maritime contract "frustration of the commercial purpose of the adventure." This happens where the ship is requisitioned by the Government before the voyage starts<sup>4</sup> or where the ship is detained at the port of loading by an order of the Government as a result of war<sup>5</sup> or where the ship cannot sail due to blockade or where the ship is lost due to no fault of the carrier and so on. Where the contract becomes

<sup>1</sup> Scrutton on Charterparties and Bills of Lading, 12th ed. p. 107.

<sup>2</sup> *Mac Andrew vs. Chapple* (1866) L. R. 1 C. P. 643; *Freeman vs. Taylor* (1831), 8 Bing 124.

<sup>3</sup> *Ibid.*

<sup>4</sup> *Bank Line vs. Capel* (1919) A.C. 435.

<sup>5</sup> *British Navigation Co. vs. Sonter* (1917) 1 K.B. 222.

impossible of performance, the rights and obligations of both parties come to an end excepting that any party who has received any benefit under the contract, is bound to restore it to the other party under the Indian Contract Act.<sup>1</sup>

(3) *Implied warranty against deviation* :—In the absence of any express stipulation, the shipowner under a contract of affreightment, impliedly undertakes to proceed in the ship without unnecessary deviation from the proper route of the voyage.<sup>2</sup> Where the route is fixed by the contract, the route so fixed is the proper route. Where no route is fixed by the contract, the usual and customary route from the port of loading to the port of discharge could be the proper route<sup>3</sup> and this need not necessarily be the shortest route.

Express stipulations authorising deviation are usually inserted in a charterparty or a bill of lading e.g., the ship may have "liberty to call at any ports in any order to sail without pilots, and to tow and assist vessels in distress, and to deviate for the purpose of saving life or property". A clause giving the ship "liberty to call at any ports in any order" is, however, construed strictly and allows the shipowners to call at such ports only as are in the ordinary course of the named voyage. Any clause giving the ship liberty to deviate is always construed with reference to the commercial object of the voyage and however wide the clause may be, it will not justify any deviation inconsistent with the main object of the voyage.<sup>4</sup>

Deviation may also be justified under the common law in the following cases :—

- (a) Where the ship deviates to save human life, as from a wrecked or torpedoed ship lying outside the ordinary route, but not for the purpose of saving property apart from agreement.<sup>5</sup>
- (b) Where the ship deviates in order to avoid some imminent peril, as by hostile capture, pirates, icebergs, or other dangers of navigation.<sup>6</sup>

<sup>1</sup> S. 65; See the rights of parties in case of discharge by supervening impossibility.

<sup>2</sup> *Leduc vs. Ward* (1888), 20 Q.B.D. 475.

<sup>3</sup> *Ibid.*, Per Lord Esher, M.R. at p. 481.

<sup>4</sup> *Glynn vs. Marketon*, (1893) A.C. 351.

<sup>5</sup> *Scaramanga vs. Stamp*, (1890), 5 C.P.D. 295.

<sup>6</sup> *The Testatrix*, (1872), L.R. 4 P.C. 171.

(c) Where the ship deviates for repairing damage to the ship or the cargo.<sup>1</sup>

Unreasonable delay may amount to deviation as much as a departure from the usual route. Thus taking a ship in tow "has been held to be equivalent to a deviation, and rightly so, seeing that the effect is necessarily to retard the progress of the towing vessel, and thereby to prolong the risk of the voyage."<sup>2</sup>

The effect of unjustified deviation is to take away from the shipowner the protection given by the "excepted points" clause in a charterparty or a bill of lading and to annul the exceptions in the contract. The shipowner will, therefore, be liable to the charterer or the shipper as the case may be for any loss or damage which the goods sustain, unless he can show that (a) the loss or damage is caused by any of the common law exceptions, namely, the act of God or by the King's enemies, or by inherent vice of the goods and (b) that the loss or damage by one of these excepted causes was not, and could not have been occasioned by the deviation.<sup>3</sup> Practically the shipowner can hardly prove the second proposition except where the loss or damage is due to the inherent vice of the goods.

(4) *Implied warranty by shipper not to ship dangerous goods without notice*—In every contract of affreightment there is an implied warranty by the shipper that the goods he ships are not dangerous or so packed that they may be dangerous. If he ships such goods he will be liable to any person who is injured by the shipment of such dangerous goods excepting where the shipowner had notice of the dangerous character of the goods or ought to have known such dangerous character or had full opportunity of observing such dangerous character.<sup>4</sup> In such a case it will be no defence that the shipper took all reasonable care to pack the goods. In *Brass vs. Mainland*<sup>5</sup> a shipper shipped sixty casks described as "bleaching powder" apparently sufficiently packed. The powder contained chloride of lime, which corroded the casks, and damaged the rest of the cargo. It was held that in the absence

<sup>1</sup> *Phelps, James & Co vs Hill*, (1891) 1 Q.B. 605

<sup>2</sup> *Per Cockburn C J in Searamanga vs Stamp* (1880) 5 CPD at p 299

<sup>3</sup> *Morrison vs Shaw Savill*, (1916) 2 K.B. 783.

<sup>4</sup> *Bainfield vs. Gobh, etc., Transport Co.* (1910) 2 K.B. 94  
<sup>5</sup> *Ibid*, (1856), 6 E & B 470.

of notice to the shipowner of the dangerous character of the goods, the shipper was liable for the damage caused, unless the powder was so well known an article that masters of ships ought to know of its dangerous character and that it was no defence for the shipper that he had shipped the goods, packed as he received them from third parties, without negligence.

"Goods may be dangerous within this principle if owing to legal obstacles as to their carriage or discharge they may involve detention of the ship."<sup>1</sup> In *Mitchell v. Steel*<sup>2</sup>, a charterer shipped rice on a ship for carriage to a particular port. The discharge of rice at the port could only take place with the permission of the British Government. The charterer knew this, but the shipowner did not and could not have reasonably known it. In consequence the ship was delayed at the port. It was held that the charterer was liable to the shipowner for the delay.

#### The Duties and Liabilities of a Carrier by Sea under the Common Law :

A carrier by sea means the shipowner or a charterer by demise who carries goods for shippers. It cannot be laid down with any amount of certainty whether the liability of a carrier by sea is like that of a common carrier or like that of a bailee for reward only. If he has the liability of a common carrier then in the absence of any express stipulation, he will be regarded as an insurer of the goods entrusted to him and he will be liable for any loss of or damage to the goods unless caused by any of the common law exceptions, namely, (a) the act of God, or (b) king's enemies, or (c) the inherent vice of the goods or (d) a 'general average sacrifice', without any negligence or deviation on the part of the carrier<sup>1</sup>. But if he has the liability of a bailee, his duty will be to take reasonable care of the goods only and he will not be liable for any loss or damage which has not been caused by his negligence<sup>2</sup>. In the earlier cases decided in England the tendency had been to regard the liability of a carrier by sea, (whether he carries goods for all and sundry or only under a

<sup>1</sup> Scrutton on Charterparties and Bills of Lading, 12th ed. p. 119.

<sup>2</sup> (1916) 2 K.B. 610.

<sup>3</sup> *Nugent v. Smith* (1876), 1 C.P.D. 422; *Per Bowen L.J. in Pandorf v. Hamilton* (1886), 17 Q.B.D. at p. 683.

<sup>4</sup> *Morrison v. Shaw Savill*, (1916) 2 K.B. 783.

<sup>5</sup> *Nugent v. Smith*, Supra.

specific charter or on the application of private shippers only), like that of a common carrier not because he is in every case a common carrier but by reason of an alleged custom by which a carrier by sea is supposed to carry goods "at his own absolute risk, the act of God or the Queen's enemies alone excepted".<sup>1</sup> But in later cases the existence of the alleged custom has been doubted and it has been held that the liability of a common carrier would attach to such carriers by sea only as undertake to carry goods for all and sundry and are within the definition of a common carrier e.g., a shipowner who carries goods in a general ship. And shipowners, other than of general ships, i.e., those who are not common carriers, are to be regarded only as bailees and will incur liability only if any loss or damage is occasioned by his negligence to exercise reasonable care and diligence.<sup>2</sup>

It is, however, only a matter of academic interest as to whether the liability of a carrier by sea is, in the absence of any express stipulation, like that of a common carrier or a bailee; for in practice the liability of a carrier is almost always defined in a contract of affreightment whether contained in a charterparty or evidenced by a bill of lading and in the case of bills of lading issued in India the duties and liabilities of a carrier are defined by the carriage of Goods by Sea Act, 1925.

In actual practice a carrier very rarely incurs the liability of a common carrier; for the charterparty or the bill of lading under which he carries goods invariably contains excepted clauses which exempt him from liability for any loss of or damage to the goods caused by certain perils specified in the clauses unless the perils causing the loss or damage could have been avoided by his reasonable care and diligence. These excepted clauses in a maritime contract are known as "excepted perils."

#### Excepted Perils :

We have already seen that "excepted perils" refer to those clauses in a charterparty or a bill of lading which relieve the carrier of his liability for any loss of or damage to the goods intrusted to him caused by any of the perils specified in those

<sup>1</sup> Per Brett J. in Liver Alkali Co. *vs.* Johnson, (1874) L.R. 9 Ex. 338 at p. 344.

<sup>2</sup> Nugent *vs.* Smith, *Sopra*; The Xantho, (1887), 12 A.C. 503; The Baduliro, (1869), L.R. 2 A. & E. 393.

clauses. In a charterparty the "excepted perils" clauses also exonerate the charterer from his liability for failing to perform his part of the contract, e.g., loading the cargo within the specified time, as a result of any of the excepted perils. Under the common law no restriction is placed on the right of the carrier to limit his liability for carrying and delivering the goods entrusted to him in the same condition as that in which he received them by inserting any exception in the contract. As a result carriers have often been inclined to expand the 'excepted perils' clauses so as to cover almost every ground on which they might be held liable. This tendency has, however, been checked by the passing of the carriage of Goods by Sea Act, 1925, which prohibits a carrier carrying goods under a bill of lading issued in India from contracting out of his liability for negligence in performing his duties enjoined by the Act or in taking reasonable care for loading, stowing, handling or discharging the goods<sup>1</sup>. We shall discuss the effects of the carriage of Goods by Sea Act, 1925 on the liabilities of a carrier later on. Apart from the effect of the carriage of Goods by Sea Act, a carrier cannot under the exceptions claim exemption from liability for any loss or damage caused by his negligence or that of his servants or by a breach on his part of the implied warranty of seaworthiness or the implied warranty against deviation unless the exceptions in the contract expressly provide for exemption of liability arising from any of these grounds. In *Siordet v. Hall*<sup>2</sup> goods were shipped under a bill of lading containing the excepted peril, "the act of God." The captain filled the boiler of the ship with water on the night previous to the date of the sailing. As a result of frost coming on during the night, the tubes burst damaging the goods. It was held that the negligence of the Captain excluded the exception, though frost was an "act of God." Similarly in *Steel vs. State Line Steamship Co.*<sup>3</sup> goods were shipped under a bill of lading which excepted "perils whether or not arising from the negligence of the shipowner's servants, risk of craft or hull, or any damage thereto, etc." The goods were damaged as a result of seawater entering through the negligence of some of the crew in leaving a port hole insufficiently fastened. It was held that if

<sup>1</sup> Carriage of Goods by Sea Act, 1925, Art. III, 2 & 8

<sup>2</sup> (1828) 4 Bing. 607.

<sup>3</sup> (1877) L.R. 3 A.C. 72.

this were so at the beginning of the voyage, the ship was unseaworthy and the exceptions in the bill of lading did not protect the shipowner, as they do not apply till the voyage has begun.

A carrier will be protected from liability under the exceptions only if the loss or damage is proximately caused by any of the excepted perils and not otherwise. Proximate cause does not mean the last cause in a chain of causes but the direct and dominant cause, though not necessarily the last cause in point of time<sup>1</sup>. Suppose goods are shipped under a bill of lading which excepts "perils arising from fire." Goods are damaged by water poured to extinguish a fire. In this case though the last cause is the pouring of water, yet fire being the dominant cause, the shipowner will be protected under the exception.

The usual excepted perils which are provided for in a charter-party or a bill of lading are the following :—

- (a) *Perils of the Sea*—The term 'perils of the sea' has the same meaning in a maritime contract as in a marine insurance policy. We have already discussed it in connection with marine insurance. Where loss or damage occurs due to perils of the sea, the shipowner is relieved of liability if 'perils of the sea' is excepted in the contract of affreightment.
- (b) *Act of God*—We have also discussed the meaning of this term in our discussion on marine insurance.
- (c) *King's enemies*—This has also been noted in the chapter on marine insurance.
- (d) *Arrests or restraints of princes, rulers and peoples*—This has also been studied in connection with marine insurance.
- (e) *Pirates, robbers and thieves*—We have also studied this in our discussion on marine insurance.
- (f) *Barratry*—This has also been discussed in connection with marine insurance.
- (g) *Negligence of master and mariners*—This exception is engrafted in a maritime contract in order to enable the carrier to claim protection under the excepted perils even where loss of or damage to the goods entrusted

<sup>1</sup> Leyland S. S. Co. vs. Norwich Union (1918) A.C. 150

to him is caused by the negligence of the master and the crew. But this will not protect the carrier if the ship was unseaworthy at the start due to the negligence of the master or the crew<sup>1</sup>, nor would it protect the carrier if he deviates without justification unless he can show that the loss or damage would have occurred in any event<sup>2</sup>. This clause can now be inserted only in a charterparty; for under the carriage of goods by Sea Act, a shipowner under a bill of lading cannot contract out for the negligence of his servants in performing the duties imposed by the Act and in taking reasonable care for the goods entrusted to him<sup>3</sup>. But the Act exempts a carrier from liability for the neglect or default of the master, mariner, pilot, or the servants of the carrier in the navigation or in the management of the ship<sup>4</sup>.

#### Duties of a Carrier by Sea under the Carriage of Goods by Sea Act :

The Carriage of Goods by Sea Act, 1925, applies only where goods are shipped under a bill of lading whether pursuant to a charterparty or not or a similar document of title<sup>5</sup>. In the first place it defines the liability of a carrier by sea by imposing certain duties on him which the carrier cannot contract out. In the second place it defines the immunities of a carrier by sea by exempting him from liability in certain specified cases. Its object has been on the one hand to deprive the carrier of his freedom to contract out of his common law liabilities and to grant him substantial protection on the other.

The duties imposed by the Act on a carrier by sea under a bill of lading are as follows :—

- (1) The carrier is bound, beforehand at the beginning of the voyage, to exercise due diligence to—
  - (a) make the ship seaworthy;
  - (b) properly man, equip and supply the ship;

<sup>1</sup> Steel *vs.* State Steamship Co. (1877) L. R. 3 A. C. 72;

<sup>2</sup> Morrison *vs.* Shaw Savill, (1916) 2 K. B. 783.

<sup>3</sup> Art. III rr. 2 and 8;

<sup>4</sup> Art. I, r. 2 (a);

<sup>5</sup> Art. I (b).

- (c) make the holds, refrigerating and coal chambers, and all other parts of the ship in which goods are carried, fit and safe for their reception, carriage and preservation.
- (2) The carrier must properly and carefully load, handle, stow, carry, keep, care for and discharge the goods carried subject to the immunities granted to him under the Act.

**Liabilities of a Carrier by Sea under the Carriage of Goods by Sea Act and the Merchant Shipping Act, 1894 :**

Under the Carriage of Goods by Sea Act, 1925, a carrier by sea carrying goods under a bill of lading issued in India or a similar document of title is absolutely liable for any loss or damage to or in connection with goods arising from the negligence, fault or failure of the carrier in the duties and obligations imposed on him by the Act i.e., his failure to exercise due diligence to make the ship seaworthy or to take reasonable care in loading, handling, discharging or carrying the goods. Any clause in the contract of carriage which would relieve the carrier or the ship from liability for such loss or damage would be null and void<sup>1</sup>. But a carrier carrying goods otherwise than under a bill of lading, e.g., under a charterparty where no bill of lading is issued to the charterer is at liberty to enter into any agreement in any terms as to his liability for such goods whether by way of exempting his liability altogether or otherwise provided such an agreement is not illegal or contrary to public policy. As the carriage of Goods by Sea Act applies in the case of shipments covered by documents of title similar to a bill of lading, it appears that the liability of a carrier, where goods are shipped under a contract evidenced by a receipt, would be the same as where the shipment is under a bill of lading. But where goods are shipped under a contract, the terms of which are embodied in a receipt which is not negotiable and marked as such, the carrier may enter into any contract relieving his liability, whether arising from his breach of duty under the Act or not, in any terms, provided the agreement is not illegal or contrary to public policy and the goods, which are agreed to be carried, are not ordinary shipments in the ordinary

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<sup>1</sup> See <sup>2</sup> Art. III, r. 8;

course of trade but are such or the circumstances, conditions and terms of their carriage are such as would reasonably justify a special agreement e.g., articles of special value like gold or silver or the carriage of ordinary commodities in times of war or similar emergencies<sup>1</sup>.

**A carrier by sea or a shipowner carrying goods under a bill of lading or a similar document of title is entitled Protection under the carriage of Goods by Sea Act. to the following immunities under the carriage of Goods by Sea Act, 1925, unless he surrenders the immunities or agrees to increase his responsibility and liability in a greater degree than is required by the Act<sup>2</sup>:**

- (1) A carrier or shipowner is not liable for any loss or damage arising or resulting from unseaworthiness of the ship unless such loss or damage is caused by want of due diligence on the part of the carrier to make the ship seaworthy and to properly man, equip and supply the ship and to make the holds, refrigerating and coal chambers, and all other parts of the ship in which goods are carried, fit and safe for their reception, carriage and preservation. If, however, any loss or damage is caused by unseaworthiness, it is for the carrier to prove that he exercised due diligence and care<sup>3</sup>.
- (2) A carrier or a shipowner is not liable for any loss or damage arising or resulting from<sup>4</sup>-
  - (a) act, neglect, or default of the master, mariner, pilot or the servants of the carrier in the navigation or the management of the ship. Leaving the hatches of the ship uncovered whereby the cargo is damaged has been held to be neglected in management entitling the carrier to protection in *Gosse Millerd v. Canadian Government Merchant Marine*<sup>5</sup>. Management of the ship means management of the whole ship and not of any particular cargo carrying apparatus e.g., the holder or refrigerator. The

<sup>1</sup> Article VI.

<sup>2</sup> Art. V;

<sup>3</sup> Art. IV, r. 1.

<sup>4</sup> Art. IV, r. 2.

<sup>5</sup> (1928) 1 R.B. 717 C.A.

carrier could be liable for any loss or damage arising from the mismanagement of such apparatus<sup>1</sup>. Similarly the stealing of cargo by the crew would not be an act of management and the carrier will not be protected<sup>2</sup>.

- (b) Fire unless caused by the fault, or privity of the carrier. It seems that the carrier will not be protected if it is caused by the negligence of the carrier to make the ship seaworthy<sup>3</sup>.
- (c) Perils, dangers and accidents of the sea or other navigable waters. We have already seen that perils of the sea do not mean every peril which may occur on the sea but mean perils of and due to the sea.
- (d) Act of God e.g., a tempest.
- (e) Act of War.
- (f) Act of public enemies.
- (g) Arrest or restraint of princes, rulers or people, or service under legal process.
- (h) Quarantine restriction.
- (i) Act or omission of the shipper or owner of the goods, his agent or representative.
- (j) Strikes or lock-outs or stoppage, or restraint of labour from whatever cause, whether partial or general.
- (k) Riots and civil commotions.
- (l) Saving or attempting to save life or property at sea
- (m) Wastage in bulk or weight or any other loss or damage arising from inherent defect, quality or vice of the goods.
- (n) Insufficiency of packing. This, of course, will not protect a carrier as against an indorsee of the bill of lading if the insufficiency was apparent when the goods were delivered to him<sup>4</sup>.
- (o) Insufficiency or inadequacy of marks.

<sup>1</sup> *Forman and Ellaens vs. Federal S. N. Co.* (1928) 2 K.B. 424.

<sup>2</sup> *R. J. Brown & Co. vs. T. & J. Harrison* (1927) 96 L.J.K.B. 1025.

<sup>3</sup> *Royal Exchange Assurance vs. Kingsley Navigation Co.* (1923) A.C. 235 where a similar provision in the Canadian Carriage of Goods by Water Act, 1910 came to be decided.

<sup>4</sup> *Silver vs. Ocean S. S. Co.* (1930) 1 K.B. 416.

- (p) Latent defects not discoverable by due diligence.
- (q) Any other cause arising without the actual fault of the carrier or<sup>1</sup> without the fault or neglect of his agents, but the carrier has to prove that the loss or damage was not caused by his fault or by the fault or neglect of his agents.

(3) A carrier is not liable for any loss or damage resulting from any deviation in saving or attempting to save life or property at sea or from any other reasonable deviation<sup>2</sup>.

(4) A carrier or a shipowner will not in any event be liable for any loss or damage to goods in any amount exceeding £100/- per package or unit, or the equivalent of that sum in any other currency, unless the nature and value of such goods have been declared by the shipper before shipment and inserted in the bill of lading. By agreement between the carrier and the shipper the maximum of £100/-, payable by the carrier where goods exceeding that value are not declared, may be increased but not reduced. The declaration required by the Act in order to make the carrier liable for any sum greater than £100/- is *prima facie* evidence of the truth of the facts contained therein but is not conclusive against the carrier who is at liberty to prove that the goods were not in fact of the declared value or nature in case any loss or damage is caused to the goods and claims are made against the carrier on the basis of the declared value. If the nature and value of the goods have been knowingly misstated by the shipper in the bill of lading the carrier will not be liable in any event for loss or damage<sup>3</sup>.

(5) Goods of inflammable, explosive or dangerous nature, which have been shipped without the knowledge and consent of the carrier, may be landed at any place at any time prior to their discharge or destroyed or rendered innocuous by the carrier without compensation, and the shipper of such goods is liable for all damages and expenses directly or indirectly arising out of or resulting from such shipment. Even if such goods are shipped with the knowledge and consent of the carrier, his master, or agent, the carrier may, if they become a danger to the ship or

<sup>1</sup> It should be read as "and"—See L. J. Brown & Co. *vs.* T. & J. Harrison (1927) 96 L.J.K.B. 1025.

<sup>2</sup> Art. IV, r. 4.

<sup>3</sup> Art. IV, r. 5.

cargo, land them at any place or destroy or make them innocuous without liability on the part of the carrier except the liability to contribute to a general average loss where they are destroyed or sold at an under value before discharge<sup>1</sup>

(6) Unless notice of any loss or damage and the general nature of such loss or damage be given in writing to the carrier or his agent at the port of discharge before or at the time of the removal of the goods or if the loss or damage be not apparent, within three days, such removal shall be *prima facie* evidence of the delivery by the carrier of the goods as described in the bill of lading excepting where there has been a joint survey and inspection at the time of removal. In any event the carrier is discharged from all liability in respect of loss or damage unless a suit is brought within one year after the delivery of the goods or the date when the goods should have been delivered. In the case of any actual or apprehended loss or damage, the carrier and the person who receives the goods must give all reasonable facilities to each other for inspecting and tallying the goods -

The Merchant Shipping Act, 1894 is an Act of the British Parliament Sections 502 and 503 give certain protection under the Merchant Shipping Act, 1894 to shipowners, British and Foreign, which applies to the whole of the British Empire<sup>2</sup> and the carriage of Goods by Sea Act does not affect or alter it<sup>3</sup>. Shipowners include a charterer by demise but not an ordinary charterer who enters into contracts of carriage with shippers. The immunities granted by the Merchant and Shipping Act, 1894, may be enumerated as follows —

(1) The owner of a British sea-going ship or of any share therein is not liable for any loss or damage happening without his actual fault or privity in the following cases, namely,<sup>4</sup>

(a) Where any goods are lost or damaged by reason of fire on board the ship; or

<sup>1</sup> Art IV, 46

<sup>2</sup> Art III, r 6

<sup>3</sup> Merchant and Shipping Act, 1894, S 509

<sup>4</sup> S 7 (1)

<sup>5</sup> The Steam Happer, No 66, (1908) A C 126, Merchant and Shipping Act, 1906, S 71.

<sup>6</sup> S 502.

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(b) where any gold, silver, diamonds, watches, jewels, or precious stones, the true nature and value of which have not been declared by the owner or shipper thereof to the owner or master of the ship in the bills of Lading or otherwise in writing, are taken in or put on board the ship and are lost or damaged by reason of any robbery, embezzlement, making away with, or secreting thereof.

(2) The owners of a ship, British or foreign, are not liable to damages beyond the maximum amounts mentioned below where such damages are caused without their actual fault or privity in any one of the following cases, namely<sup>1</sup> —

- (a) where any loss of life or personal injury is caused to any person carried in the ship or
- (b) where any loss of life or personal injury is caused to any person carried in any other vessel due to the improper navigation of the ship ;
- (c) Where any damage or loss is caused to any goods, merchandise or other things whatsoever,- on board the ship ;
- (d) where any damage or loss is caused to any other vessel, or to any goods, merchandise, or other things whatsoever on board any other vessel, due to the improper navigation of the ship ,

The maximum amount payable by the owners of the ship as compensation is the amount calculated at £15/- for each ton of the ship's tonnage where loss of life or personal injury is caused either alone or together with loss or damage to vessels, goods merchandise or other things. But where there is loss of life or personal injury together with loss of goods, vessels etc., the claimants for loss of life or personal injury are alone entitled to a maximum amount calculated at £7/- per ton of the ship's tonnage out of the total maximum of £15/- per ton of the ship's tonnage and the remaining part of £8/- per ton of the ship's tonnage is the maximum payable to the claimants for loss of or damage to goods, vessels, etc. But if the loss of life or personal injury is assessed by the court at an amount exceeding the

<sup>1</sup> S. 503 (1), (a), (b), (c) & (d)

<sup>2</sup> S. 503 (1), (i) & (u).

maximum calculated at £7/- per ton of the ship's tonnage, the claimants for such loss will be entitled to a proportionate share in the residue i.e., in the £8/- share of the total maximum calculated at £15/- per ton of the ship's tonnage.<sup>1</sup> It seems that if the loss of life or personal injury is assessed at less than the £7/- share, the claimants for the loss of goods, vessels etc., cannot claim in the residue of that share which will enure to the benefit of the owners of the ship. Where there is loss of life or personal injury only, the claimants for such loss are entitled to claim upto the maximum amount calculated at £15/- per ton of the ship's tonnage. But if such loss is assessed at less than the maximum the claimants cannot claim anything more than the assessed amount. Where there is loss or damage to goods, vessels, merchandise etc., the claimants for such loss cannot get more than a maximum amount calculated at £8/- per ton of the ship's tonnage.<sup>2</sup> The following example will make the position clear.

The owners of a ship, X, weigh 1000 tons. Due to bad navigation it collides against another ship Y, as a result of which Y sinks along with her cargo. The value of Y is, £20,000/- and that of her cargo Rs. 20,000/-. The total loss is, therefore, Rs. 40,000/. As the loss is only of goods and the vessel, the owners of X will have to pay Rs. 8000/- only i.e. the maximum amount calculated at £8/- per ton of the ship's tonnage of 1000 tons.

Thus Rs. 8000/- will be paid as between the owners of Y and those of her cargo proportionately i.e. Rs. 4000/- to the owners of Y and Rs. 4000/- to the owners of her cargo. But suppose in addition to this loss seven lives on board of both X and Y are lost. The owners of X will then be liable to a maximum compensation of £15,000/- calculated at £15/- per ton of the ship's tonnage. Out of this £15,000/- the claimants for the loss of the lives will be entitled at once to £7000/-, being the £7/- part of it. If the loss of lives is assessed by the court at £7000/-, the claimants in respect thereof will have no further claim on the residue. If it is assessed at less than £7000/-, say £5000/-, the remaining £2000/- out of £7000/- will go to the benefit of the owners of X and not to the owners of Y or those of her cargo. But if the loss of lives is assessed at more than £7000/-, say,

<sup>1</sup> *The Victoria* (1888), 13 P. D. 125; see also *The Corathie*, (1897)

p. 178.

<sup>2</sup> § 503 (1), (a).

£17,000/-, then the claimants thereof will be entitled to a proportionate share in the remaining £8/- part of the total of £15,000/- i.e., £800/- for the unsatisfied balance of £10,000/- along with the claims of the owners of Y and those of her cargo. The residue after paying off £7000/- to the claimants for the loss of lives is £8000/-. On this £8000/- the owners of Y, the owners of her cargo, and the claimants for the loss of lives have their respective claims for £20,000/-, £20,000/- and Rs. 10,000/- (being the unsatisfied balance for the compensation payable for the loss of lives).

The total of these claims is £50,000/- of which 2/5th is that of the owners of Y, 2/5th is that of the owners of the cargo and 1/5th is that of the claimants for the loss of lives for the unsatisfied balance. Therefore, the owners of Y will get a proportionate 2/5th share of £8000, i.e., £3200/-, the owners of her cargo will get the same amount of £3200/- and the claimants for the loss of lives will get a proportionate 1/5th share of £8000, i.e., £1600/-. That is out of the total maximum amount payable by the ship-owners namely £15,000/- £8000/- will go to the claimants for the loss of lives, £3200/- will go to the owners of Y and £3200/- will go to the owners of her cargo. But suppose there is no loss of vessel or cargo but a loss of only two lives. The court will assess the damage for the loss of each one of these lives by taking into consideration all relevant circumstances, namely, the age of the deceased, his expectation of life, the number of his dependents, the means of livelihood of his dependents and so on. Suppose, of the two lives one was an old man with hardly many years to live and having only one dependent, namely, a widow who has sufficient means to maintain herself and the other was a young man who had many dependents without any other means of livelihood excepting the income earned by him. The court will assess a greater damage for the loss of the young man's life than that for the old man's life. Suppose the court assesses £20,000/- for the loss of the young man's life and £10,000/- for that of the old man's life. The total loss is then £30,000/- of which 2/3rds will go to the claimants for the loss of the youngman's life and 1/3rd to that for the loss of the oldman's life. The maximum amount payable by the owners of X is £15,000/-, calculated at £15/- per ton of the ship's tonnage of 1000 tons. Therefore the claimants for the loss of the youngman's life will get a proportionate 2/3rd share of the £15,000/- i.e. £10,000/- and the claimant for the loss

of the old man's life will get a proportionate 1/3rd share of the £15,000/- i.e., £5,000/-.

### Clauses in a Charterparty :

A charterparty, as we have already seen, is itself the contract of affreightment. It usually sets out in detail the duties of the charterer and the shipowner. The performance of the contract by the shipowner and the charterer takes place after the signing of the charterparty. The following are the usual clauses in a charter party :-

(a) *Proceeding to the place of loading* : This clause imposes duty on the shipowner to proceed to the place of loading. The port to which the ship is to proceed may be named in the charter or it may be left to the charterer to name, being "a port as ordered". Where the port is named in the charter or is named afterwards by the charterer, the ship is bound to go there for the purpose of loading the cargo furnished by the charterer, even if the ship cannot get to the port or the port is unsafe, unless the charter-party contains a stipulation that the ship is to proceed to the port or as near as she can safely get or that the port is a "safe port". A "safe port" means a port which is not only physically safe for the ship to get to but also politically safe.<sup>1</sup> The shipowner will fulfil his obligation if the ship gets to the port or as near as she can safely get or to any safe port where the charter-party permits the same. As to the time within which the ship is required to reach the port of loading, charterparty usually provides that the ship should reach the port of loading either by a fixed date or with reasonable or all convenient speed. Where the charter-party is silent on this point, the shipowner is nevertheless bound to exercise due diligence to reach the port with reasonable or convenient speed.<sup>2</sup> If the shipowner fails to bring the ship to the port of loading or as near thereto as she can safely get or to any other safe port, as the case may be, within the fixed day, where the day is fixed or within a reasonable time, where no day is fixed the charterer can, in all cases, except where the delay is caused by any of the excepted perils specified in the charterparty, recover damages suffered by him for the delay.<sup>3</sup> But whether such delay

<sup>1</sup> *The Teutonia* (1872), L. R. 4 P. C. 171 at pp. 181, 182.

<sup>2</sup> *MacAndrew vs. Chapple* (1865), L. R. 1 C. P. 643.

<sup>3</sup> *Barker vs. MacAndrew* (1865), 18 C. B. N. S. 759.

will entitle the charterer to cancel the contract and refuse to load depends on whether the delay is so inordinate as to amount to a frustration of the commercial adventure embodied in the charter-party.<sup>1</sup> If the delay is not such as to defeat the commercial object of the adventure, the charterer cannot throw up the charter and he will have to rely on such remedies as he may have by way of damages unless the delay is brought about by an excepted peril.<sup>2</sup> In *Hudson vs. Hill*<sup>3</sup> a ship was chartered on 28th December, while lying at U, to proceed forthwith to X, and there load, perils excepted "which may prevent the loading or delivery of the cargoes during the said voyage." Owing to delays caused by excepted perils, the ship did not reach X till 28th July whereupon the charterers refused to load. It was found as a fact that the delay did not defeat the commercial object of the adventure. It was accordingly held that "forthwith" meant without the reasonable delay; that the exceptions applied to the voyage to the port of loading and that the charterers were not justified in cancelling the charter. In order to protect the charterer, it is usual to have a "cancelling clause" in the charterparty which entitles the charterer to cancel the contract on the failure of the ship to reach the port within the fixed date or within a reasonable time where no date is fixed. Where there is a cancelling clause in case of delay which is such as to defeat the object of the adventure, the charterer can cancel the contract even if the delay is brought about by an excepted peril. In *Smith vs. Dart*<sup>4</sup>, a ship was chartered to proceed to a port and there load, certain perils being excepted, the charterer having the right to cancel the charter if the ship did not reach the port of loading and be ready to load by 15th December. Through excepted perils, the ship could not be ready to load on 15th December. It was held that the charterer was entitled to cancel the contract. The charterer may in addition to cancelling the charter, where he is entitled to do so, sue the shipowner for damages caused by the delay unless it is brought about by excepted perils.<sup>5</sup> The charterer may, on the otherhand, where he is entitled to cancel the charter, elect to affirm it and load his cargo

<sup>1</sup> *Jackson vs. Union Marine Insurance Co.* (1874) L. R. 10 C. P. 125;

<sup>2</sup> *Barker vs. MacAndrew* (1867), 18 C. B. N. S. 759;

<sup>3</sup> (1874), 43 L. J. C. P. 273;

<sup>4</sup> (1884), 14 Q.B.D. 105.

<sup>5</sup> *Nelson vs. Dundee East Coast S. S. Co.* (1907), *Sea. Cas.* 927.

and sue the shipowner for damages caused by the delay unless it is brought about by an excepted peril.<sup>1</sup>

(b) *The loading of the cargo* :—This clause imposes the duty on the charterer to load the cargo. When the ship is at the place where she is bound to be i.e., either at the port or as near thereto as she can safely get as the case may be, and the charterer has been notified about the readiness of the ship to load, the ship is regarded as an *arrived ship*. The obligation of the charterer to load begins only after the ship becomes an arrived ship. In the absence of any stipulation to the contrary, the duty of the charterer to supply cargo according to the charter is absolute. This duty is threefold, namely, (a) the cargo must reasonably comply with the terms of the charter, (b) the charterer must bring the cargo to the loading place, if it is not already there and (c) the charterer must perform his part of the actual loading, if any.

As regards (a) the duty of the charterer is to load the kind of cargo specified in the charterparty if any. If he loads a cargo of different description whose freight is higher than that of the chartered freight, the shipowner can claim the excess freight. In *Steven vs. Bromley*<sup>2</sup> a ship was chartered to load at New York a cargo of steel billets at 23sh. a ton. The charterer shipped 1208 tons of Steel billets and 987 tons of other goods, the market rate of freight for which was higher than 23 sh. a ton. It was held that the shipowner was entitled to the higher rate of freight on the 987 tons. Where the charterer has the option to load alternative cargoes e.g., a full cargo of "wheat and/or maize and/or rye", the charterer will not be relieved of liability if he is prevented from loading one kind of cargo e.g., wheat by an excepted peril ; for he can as well load either maize or rye.<sup>3</sup>

As regards (b) the duty of the charterer is to bring the goods to the place of loading, and in the absence of any agreement or custom of the port, to the side of the ship. This duty is absolute and the excepted perils in the charterparty do not apply to the bringing of the cargo to the port of loading, but applies to the operation of putting the cargo on board only<sup>4</sup>. The charterer will not, therefore, be relieved of his liability of bringing the cargo to

<sup>1</sup> *Barker vs. MacAndrew*, *Supra*.

<sup>2</sup> (1919) 2 K.B. 722.

<sup>3</sup> *Brightman vs. Bunge Y. Born*, (1924) 2 K.B. 619.

<sup>4</sup> *Coverdale vs. Grant* (1884) 9 A.C. 470.

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the port of loading even if he is prevented from doing so by circumstances beyond his control e.g., strikes,<sup>1</sup> bankruptcy of merchants supplying the cargo,<sup>2</sup> non-existence of such cargo,<sup>3</sup> or impossibility of carrying the cargo, when obtained, to the port of loading due to ice, railway delays or Government orders.<sup>4</sup> For failing to provide the cargo or any part of it the charterer is liable to pay compensation or damage to the shipowner equivalent to the freight lost thereon. But the charterer is relieved from this liability in the following cases:—

- (i) If the charterparty provides expressly for any exception in bringing the cargo to the port of loading and the charterer is prevented from bringing the cargo by reason of the excepted cause.
- (ii) If the charterparty contains an implied exception excusing the charterer from liability for failing to bring the cargo to the port of loading and the charterer is prevented from bringing the cargo by the excepted event. Thus if the cargo must necessarily be conveyed from a particular place in a particular manner, an exception will be implied that if the transit is prevented by an excepted peril expressly mentioned in the charter, the charterer will not be liable provided he can show that there was no other method of bringing the cargo to the port of loading.

In *Hudson v. Fdte.*,<sup>5</sup> a ship was chartered to load grain at a particular port, the cargo to be brought alongside the ship at the port of loading and loaded within thirty days, delay in loading being excepted in case it was caused by ice. The charterer would not load the ship within the fixed time as a result of the river through which the grain was to have been brought to the port of loading being blocked by ice. In an action by the ship-owner for damages for detention of the ship beyond the stipulated period, it was found that the only method by which the grain could have been brought to the port

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<sup>1</sup> *Ibid.*, p. 476, per Lord Selbourne

<sup>2</sup> *Ibid.*

<sup>3</sup> *Hills v. Sughrue* (1846), 15 M. & W. 253.

<sup>4</sup> *Coverdale v. Grant*, Supra.

<sup>5</sup> (1868), L.R. 3 Q.B. 412

of loading was the transit by the river. It was accordingly held that the transit being rendered impossible by an excepted peril, namely, ice, the charterer was not liable for the delay.

(iii) If both the charterer and the shipowner knew that the cargo would have to be obtained from a particular source or under certain circumstances which might cause delay in obtaining it and such delay in fact occurs.<sup>1</sup> In *Harris v. Drusman*<sup>2</sup> ship was chartered to load at a particular colliery. Before signing the charterparty both parties knew that the colliery engine had broken down and was being repaired. It was held that the charterer would not be liable in case of delay in bringing the cargo provided the engine was repaired and the cargo was loaded within a reasonable time.

As regards (c) the duty of the charterer ceases as soon as he brings the goods by the side of the ship and in the absence of any special custom or agreement, the duty of putting them on board and stowing them is on the shipowner, who is liable for any loss or damage caused by his negligence or that of the stevedore employed.<sup>3</sup> But if the charterparty provides for anything to be done by the charterer, the charterer is liable for his failure to do it unless he is excused by the excepted perils mentioned in the charterparty. The excepted perils apply to the operations connected with putting the goods on board the ship, as we have already noticed.

A charterparty usually provides that the charterer is to load a certain number of tons or a "full and complete cargo" either of specified goods or goods in general. Where the charterer is to load a full and complete cargo, the duty of the charterer is to load as much cargo as the ship can carry with safety,<sup>4</sup> subject to modification which any custom of the port of loading may impose.<sup>5</sup> Thus where the goods are of such a nature that they cannot be loaded without having spaces in the ship's holds known as "broken Stowage" e.g., when sugar or molasses are loaded in

<sup>1</sup> Ardan S. S. Co. *v. Wier* (1905) A.C. 501.

<sup>2</sup> (1854), 23 L.J. Ex. 210.

<sup>3</sup> Blaikie *v. Stembridge* (1859), 6 C.B.N.S. 894.

<sup>4</sup> Heathfield *v. Rodenacher* (1896), 2 Com. Cas. 55 (C.A.).

<sup>5</sup> Cuthbert *v. Cumming* (1856), 11 Ex. 405.

bogheads and puncheons respectively leaving broken stowage, the broken stowage has to be filled up by the charterer unless he is exempted from doing so by the custom of the port of loading.<sup>1</sup>

(c) *Cesser Clause* :—This clause provides that the liabilities of the charterer under the charterparty will cease on the cargo being shipped and is usually inserted in consideration of the charterer granting to the shipowner a lien on the cargo for demurrage and dead freight. The exemption granted to the charterer is co-extensive with the lien conferred on the shipowner and charterer, inspite of the clause, remains liable for claims for which no lien is granted to the shipowner.<sup>2</sup> Thus where in a charterparty shipowner was given a lien on the cargo for demurrage only and not for damages for detention,<sup>3</sup> and the charterer was relieved from liability on the cargo being loaded, it was held that the charterer was liable for damages for detention, but not for demurrage for which the shipowner was given a lien.<sup>4</sup>

(d) *Unloading or discharge of the cargo* :—This clause provides for the duty of the shipowner to proceed with his ship to the port of discharge and arrange for the discharge of the cargo. In the absence of any special agreement or custom the duty of the shipowner is to get the goods out of the ship's hold and place them on the ship's deck or alongside<sup>5</sup> and he is not bound to give notice of his readiness to unload either to the charterers, or to shippers or consignees under bills of lading.<sup>6</sup> The duty of having the cargo unloaded after it has been taken out of the ship's hold is, in the absence of agreement or custom, on the charterer or the shipper.<sup>7</sup> If no time is fixed by the charterparty or the bill of lading the consignee is entitled to a reasonable time for unloading his cargo.<sup>8</sup> But the matter is invariably governed either by agreement, custom, or by statute.

Where goods belonging to different shippers get mixed up so

<sup>1</sup> *Cuthbert vs. Cumming*, (1856) 11 Ex. 405

<sup>2</sup> *Hansen vs. Harrold*, (1894) 1 Q.B. 612.

<sup>3</sup> See *infra* for difference between demurrage and damages for detention

<sup>4</sup> *Francesco vs. Marsey*, (1873) L.R. 8 Ex. 101.

<sup>5</sup> *Bellantyne vs. Paton*, (1912) Sess. Cas. 246.

<sup>6</sup> *Harman vs. Mart*, (1815) 4 Camp. 161.

<sup>7</sup> *Postlethwaite vs. Freeland*, (1880) 5 A.C. at p. 608, per Lord Selborne

<sup>8</sup> *Bourne vs. Ratliff*, (1844) 11 Cl. & Fin. 45 at p. 70.

as to become unidentifiable during the voyage due to the fault of the shipowner, the shipowner is liable for any loss which the shipper may suffer. But if such an event is caused by excepted perils, the shipowner is not liable and the owners of the mixed-up goods become tenants-in-common of the entire quantity of mixed goods in the proportions to which they have severally contributed to that whole<sup>1</sup> and the shipowner must deliver the whole or the proceeds thereof in such proportions.<sup>2</sup>

(e) *Demurrage* :—A charterparty usually contains the demurrage clause which provides that the charterer will have to finish the loading or unloading within a fixed time or at a fixed rate, e.g., 200 tons per day, from which the time required can be easily ascertained and in default to pay an agreed sum per day upto a fixed number of days or for each day the ship is delayed after the fixed time. The time so fixed for loading or unloading is known as *lay days*. Where no time is fixed or where the charterer is required to load and unload "with customary despatch" or similar terms, the duty of the charterer is to complete the work within a time which is reasonable having regard to the circumstances existing at the place of loading or unloading, and the custom of the port.<sup>3</sup>

"Demurrage, in its strict meaning, is a sum agreed by the charterer to be paid as liquidated damage for delay beyond a stipulated or reasonable time for loading and unloading".<sup>4</sup> The stipulation as to the payment of liquidated damages is called *exhaustive* when the charterer agrees to pay a liquidated amount by way of compensation for delay for each day's delay upto a reasonable time after the expiry of the lay days, where the lay days are fixed or after the expiry of a reasonable time where the lay days are not fixed e.g., "ten days for loading (or loading with customary despatch) and demurrage at £20/- per diem afterwards", which covers all delay upto a reasonable time. The stipulation is called partial when the liquidated amount is to be paid for each day's delay upto a specified number of days after the expiry of the lay days or of a reasonable time according as whether the lay days are fixed or not e.g., "ten days to load, (or loading with

<sup>1</sup> Spence *vs.* Union Marine Co., (1868) L.R. 3 C.P. 427.

<sup>2</sup> Scrutton on Charterparties & Bills of Lading, 12th ed.

<sup>3</sup> Postlethwaite *vs.* Freeland, (1880), 5 A.C. 599.

<sup>4</sup> Scrutton on Charterparties, 12th ed., p. 347.

customary despatch) ten days on demurrage at £20/- per diem" which covers delay only for the demurrage days

Where the demurrage clause is exhaustive i.e., where the demurrage days are not fixed or where the demurrage days are fixed, all delay after a reasonable time from the expiry of the lay days in the first instance and ill delay after the demurrage days in the second instance entitle the shipowner to unliquidated damages for detention Unliquidated damages for detention should be clearly distinguished from demurrage proper So long as the charterer's liability to pay demurrage continues, the charterer has the right to detain the ship on payment of the demurrage<sup>1</sup> But when the period during which the demurrage is payable expires (i.e. after the expiry of a reasonable time from the end of the lay days where the demurrage days are not fixed or after the expiry of the demurrage days where they are fixed) and the shipowner gets the right to claim damages for detention, the charterer cannot detain the ship and the ship can sail away-

Where there is a charterparty containing express stipulations as to demurrage, the following persons will be liable for demurrage

- (a) The charterer unless he is relieved of liability under a lesser clause or under a new contract evidenced by a bill of lading issued subsequently<sup>2</sup>
- (b) The parties to the bill of lading, if the charterparty stipulations as to demurrage are expressly incorporated in the bill of lading<sup>3</sup>

#### **Master of the Ship—His Duties :**

The master is the highest officer on board a ship In popular language he is known as the Captain On a voyage under a contract of affreightment the master occupies a double position, namely, (1) he is in general the agent of the shipowner in doing what is necessary to carry out the contract, and (2) he is in case of necessity and for the preservation and benefit of the cargo the agent for the cargo-owners

<sup>1</sup> Wilson & Coventry vs Thorsen, (1910) 2 K.B. 405

<sup>2</sup> Reider vs Arcos, (1929) 1 K.B. 352.

<sup>3</sup> Scrutton on Charterparties, 12th ed 369

<sup>4</sup> Ibid.

As an agent of the shipowner he has to perform all the duties of the shipowner under the charterparty and he can also deal with the ship in times of necessity or emergency as a man of ordinary prudence would do under the circumstances. Thus he signs bill of lading in favour of charterers or shippers. He has to provide necessaries which the shipowners have to provide under the charter-party. He has to proceed without unjustified deviation and unreasonable delay and has to make the ship seaworthy. He also has to take reasonable care for the goods carried on the ship unless the terms of the charterparty or the bill of lading exempt the shipowner from liability for the negligence of the master and the crew. The shipowner is liable for any loss or damage caused by the negligence of the master in fulfilling the under-taking of the shipowner or in taking reasonable care for the goods unless he is expressly exempted from such liability by the terms of the charterparty or the bill of lading. In times of emergency the master as an agent of necessity can do whatever is reasonable under the circumstances and his acts in this respect will bind the shipowner. Thus the master can order the mast to be cut off if it is necessary to save the ship or to raise money on the security of the ship where it is necessary to complete the voyage.

The master derives authority to act as an agent of the cargo owner in a manner inconsistent with the ordinary rights of the cargo-owner e.g. by selling the goods or throwing them overboard or pledging them for advances of money under two circumstances—

- (1) The necessity for the action
- (2) The impossibility of communicating with the shipowners or cargo-owners or the absence of their instructions when communication has been made to them

Thus in *The Hamburg*<sup>1</sup> a vessel bound from South America to London with a cargo belonging to English owners, but not perishable, put into St. Thomas for repair. The master without communicating with the cargo-owners raised money on a bottomry bond on ship, freight and cargo for the purpose of repair. It was found that mails left St. Thomas for London every fortnight, taking fourteen days for the journey and the master could have easily communicated to the cargo-owners and waited for their instructions in view of the fact that the cargo was

<sup>1</sup> (1863), 2 Moore, P.C.N.S. 289.

not perishable. It was, accordingly, held that the cargo owners were not bound by the bottomry-bond. It may be noted here that if the cargo were perishable then the master could not have communicated with the cargo-owner without allowing a sufficient time to lapse during which the cargo would have perished and the master would have been authorised to raise the money on the bond without communicating with the cargo owners.

### **Freight :**

"Freight" in the ordinary mercantile sense, is the reward payable to the carrier for the carriage and arrival of the goods in a merchantable condition, ready to be delivered to the merchant.<sup>1</sup> In the absence of agreement the carrier is entitled to the freight stipulated in a contract of affreightment if he has substantially performed the contract by delivering the goods in a merchantable condition.<sup>2</sup> Thus he is entitled to the freight even if the goods are delivered in a damaged condition provided the goods remain as merchantable articles of the particular description.<sup>3</sup> But no freight is payable if the goods are lost whether by reason of excepted perils or not, unless the contract of affreightment provides for advance freight or a lump sum freight or the goods are lost due to the fault of the shipper alone.<sup>4</sup> Thus a carrier cannot in the absence of express agreement claim a proportionate freight for the part of the voyage during which the goods are carried if the goods are lost and cannot be delivered at the port of destination.<sup>5</sup>

The following are the usual kinds of freight stipulated in a contract of affreightment -

(a) **Simple Freight** - This is the most common type of freight which is only payable on the delivery of the [redacted] contractual rate per unit.

(b) **Antedated Freight** - This signifies a freight which is payable at any time before the goods are delivered at the port of destination, the actual point of time when it is to be fixed in the contract. It must be paid even if the goods are lost, provided the loss occurs after the

<sup>1</sup> Scrutton v. Counterparties and Bills of Lading, 12th ed p 374.

<sup>2</sup> Per Mr. Justice Oakin in Oxley, (1864), 15 C.B.N.S 646 p 664.

<sup>3</sup> Ibid

<sup>4</sup> Carrington, (1873) L.R. 5 P.C. 134

<sup>5</sup> Mc Gregor v. Britannia Iron Works, (1877) 2 Q.B.D. 423.

due date of payment,<sup>1</sup> and if it is already paid the carrier can retain it.<sup>2</sup> It is immaterial whether the loss is caused by excepted perils or not.<sup>3</sup> Advance freight should, however, be distinguished from a loan by the shipper to the shipowner, whether on the security of the freight or not; for a loan by the shipper can be recovered from the shipowner if the cargo is lost and not delivered.<sup>4</sup> Whether a payment by the shipper is by way of advance freight or a loan is to be determined by the intention of the parties as expressed in the contract of affreightment,<sup>5</sup> but a stipulation that it shall be paid "subject to insurance" or "less insurance", will indicate that the payment is an advance of freight.<sup>6</sup>

- (c) *Dead Freight* :—This is the name given to the compensation payable to the carrier for loss of freight where the charterer fails to furnish a full cargo in terms of the charterparty.
- (d) *Lump Sum Freight* :—This is a lump or gross sum payable by the charterer for the use of the whole ship and for the entire cargo. It is, therefore, payable if the carrier is ready to perform his contract, though no goods are shipped, or though part of the goods shipped is not delivered. The carrier is entitled to payment of the lump freight agreed upon if he delivers part of the cargo, and it is immaterial whether the part remaining undelivered is lost by the excepted perils or not.<sup>7</sup> If the part remaining undelivered is lost by a cause not excepted in the charterparty the carrier will remain liable for the loss but will earn ~~dead~~ freight by delivering part of it.
- (e) *Time Freight* :—This is a kind of [redacted] which is payable for fixed periods of time at the [redacted] each period specified in the charterparty. It is [redacted] even if time

<sup>1</sup> Oriental S. S. Co. *vs.* Taylor, (1893) 2 Q.R.

<sup>2</sup> Byrne *vs.* Schiller, (1871) L.R. 6 Ex. 20, 319.

<sup>3</sup> Rodocanachi *vs.* Milburn, (1886) 18 Q.B.D.

<sup>4</sup> Watson *vs.* Shankland, (1873) L.R. 2 H.L.

<sup>5</sup> Allison *vs.* Bristol Marine Insurance Co., (1876), [redacted] 309.

<sup>6</sup> *Ibid.*

<sup>7</sup> The Norway, (1865), 3 Moore, P.C.N.S. 245.

is lost in prosecuting the voyage by the ship being unavoidably delayed for repairs or bad weather or on account of blockade or embargo unless it is provided otherwise in the charterparty or the delay is so great as to amount to a frustration of the object of the voyage<sup>1</sup>

*Persons entitled to freight*—The person entitled to receive payment of freight is *prima facie* the person with whom the contract of affreightment is made. But it may also be payable to a purchaser, or to a mortgagee, of the ship or it may be assigned and made payable in favour of a third person.

*Liability for freight*—The primary liability for the payment of freight is on the shipper or the charterer. But under the English Bills of Lading Act, 1855 section 10(1) the indorsee of a bill of lading to whom the property in the goods has passed becomes liable for the payment of freight. Apart from this statutory liability, *contra* the indorsee of a bill of lading who takes delivery of goods by presenting a bill of lading under which freight is payable becomes liable to pay the freight on an implied agreement to do so the same to be inferred from the circumstances.<sup>2</sup>

*Shipowner's lien for freight*—A shipowner has a lien at common law on the cargo carried by him for the freight due thereon. But this lien subsists only for freight payable on delivery of cargo and does not extend to advance freight or dead freight or demurrage. In exercise of his lien the shipowner is entitled to retain the cargo until the freight is paid.

#### General average loss and particular average loss:

We have discussed this subject in connection with marine insurance. So if the reader reads subject matter of the contract of affreightment instead of the subject matter insured in connection with our discussion on the subject under the chapter on marine insurance nothing more need be said here on the subject.

<sup>1</sup> Scrutted on Charterparties 12th ed. p. 403. See also Havelock *vs* Geddes, (1889), 10 East, 555 and Moorsone *vs* Greaves, (1811), 2 Camp 626.

<sup>2</sup> Smith's Mercantile Law 13th ed., p. 385.

<sup>3</sup> Sanders *vs* Vanzeller (1843) 12 L.J. Ex. 497; Furness *vs* White, (1885) A.C. 40.

### **Bottomry and Respondentia :**

Where the shipowner obtains advances for the use of the ship on the security of the ship, freight and cargo, the contract whereby such advances are obtained is known as the "bottomry". Where such advances are obtained on the security of cargo only, the contract is known as "respondentia". The characteristic features of a bottomry or respondentia are as follows .—

- (a) The contract must be in writing.<sup>1</sup> Where a bottomry is executed in the form of a bond,<sup>2</sup> it is known as "bottomry bond". Where a bottomry is executed in the form of a deed poll<sup>3</sup> it is known as "bottomry bill".
- (b) The contract has the effect of hypothecating the ship, freight and cargo in the case of bottomry and cargo only in the case of respondentia as security for repayment of the loan.
- (c) The money advanced on bottomry or respondentia is repayable only on the safe arrival of the ship or cargo at its destination and not otherwise. The essence of a bottomry or respondentia is that there must be a maritime risk involved so that the borrower is relieved of his liability in case the ship or the cargo which is the security for the loan is lost before arrival at destination.
- (d) The amount of the loan, the interest to be paid, the property hypothecated for repayment of the loan and the fact that repayment depends upon the safe arrival of the ship or cargo at its destination must be stated specifically in the charterparty.
- (e) The contracts of bottomry and respondentia are usually entered into by the master under an implied authority as the agent if necessary on the owner of the ship or

<sup>1</sup> Ex Parte Halkett (1815), 3 Ves. & R. 135.

<sup>2</sup> A bond is a deed signed and sealed by only one party to the contract whereby he binds himself to pay another a certain sum of money followed by certain conditions of repayment.

<sup>3</sup> When there is only one party to a deed, as when a deed consists merely of a promise by A to B without any promise by B to A, the deed is called a deed poll.

<sup>4</sup> Price *vs.* Maritime Int. Co., (1901) 2 K.B. 412; *The Mary Ann*, (1863) 1 R. 1 A. & E. at p. 14.

<sup>5</sup> *The Heinrich Bjorn*, (1885), 10 P.D. 44, 49.

cargo. The authority of the master to hypothecate the ship or cargo arises in the following circumstances.<sup>1</sup> (1) Where assistance is required for prosecuting the voyage and the voyage would be frustrated if no assistance is procured and there are no other resources at hand e.g., when the master has to pay to free the ship from arrest for salvage; (2) it is impossible to communicate with the owner to get his consent and (3) it is not possible to raise money on better terms or in any other manner. But where the master can communicate with the owner<sup>2</sup> or the owner has an agent who is willing to advance money<sup>3</sup> or the money can be raised on the personal security of the owner on better terms,<sup>4</sup> the master has no authority to enter into a bottomry or respondentia without the consent of the owner. If he does so the bottomry or respondentia will be void as against the owner.

#### **Rights of a holder of bottomry or respondentia :**

The lender on a bottomry or respondentia has a 'maritime lien' on the hypothecated ship or cargo. If the money is not repaid within the time prescribed the lender may institute an Admiralty action for the arrest of the ship or the cargo and its sale.<sup>5</sup> Where the same ship or cargo is hypothecated more than once during the same voyage the last hypothecator<sup>6</sup> prior claim on the sale proceeds of the ship or cargo<sup>7</sup> over hypothecatees on the principle that the last loan<sup>8</sup> is the means of preserving the ship, and without it, the former<sup>9</sup> lenders would have entirely lost their security.<sup>10</sup> The holder of a bottomry or respondentia, however, loses all claim against the owner of the ship or cargo if it fails to arrive at its destination safely.

<sup>1</sup> The Jersey (1817), 3 Hagg. Adm. Rep. 404; The Karnak (1869), L.R. 2 P.C. 505.

<sup>2</sup> The Oriental (1851), 7 Moo. P.C. Cas. 398.

<sup>3</sup> Gunn *vs.* Roberts, (1874), L.R. 9 C.P. 331.

<sup>4</sup> Heathorn *vs.* Darling, (1836) 1 Moo. P.C. Cas. 5.

<sup>5</sup> See Williams and Bruce, Admiralty Practice, Part II, for the procedure in such actions.

<sup>6</sup> The Eliza (1833), 3 Hagg. Adm. Rep. 87.

**Distinction between a bottomry or respondentia and other forms of security :**

We have already dealt with the different forms of securities, namely, mortgage, hypothecation, lien, and pledge.<sup>1</sup> A bottomry or respondentia differs from an ordinary mortgage or hypothecation in that the money lent on a bottomry or respondentia is in hazard during the voyage; so that if the ship or cargo does not arrive safely at its destination nothing is repayable.<sup>2</sup> It also differs from a pawn or pledge in that it is not necessary that the lender should take possession of the ship or cargo. It also differs from the other forms of securities in that if there are successive lenders, the last in point of time is entitled to priority of payment.<sup>3</sup> It is worthy of note that in the other cases of securities the prior lender has a prior right. There is also another practical difference between a bottomry or respondentia and other forms of securities. Since the money lent on a bottomry or respondentia is in danger of being lost in case the ship or cargo fails to reach its destination the rate of interest is always excessively high.

<sup>1</sup> See p. 387 supra.

<sup>2</sup> *Stainbank vs Fenning* (1951) 20 L & C P 226. *The Haabet* (1909) p. 295.

<sup>3</sup> See Supra.

## CHAPTER XI

### BANKERS & BANKING

The law relating to bankers and banking may be divided into two distinct branches, namely, (a) the law regulating the business of banking i.e. relations between bankers and their customers and between bankers and the outside world which we may for the sake of convenience call the pure law of banking and (b) the law regulating the organic side of bankers as an institution. The former deals with matters like the payment and collection of cheques and other negotiable instruments and the rights and obligations of bankers in respect thereof both in relation to their customers as well as to members of the general public. The latter deals with matters like the incorporation, management and dissolution of banking concerns. Until the passing of the Negotiable Instruments Act of 1881 there was no Statute in India containing provisions applicable to the business of banking exclusively. The law of banking meant nothing more than the common law of England relating to banking subject to the provisions of the Indian Contract Act 1872. Then came the Negotiable Instruments Act with its specific provisions relating to the payment and collection of cheques by a banker. But the Indian Contract Act and the Negotiable Instruments Act do not exhaust the whole field of banking law and recourse has, therefore, to be taken frequently to the common law of England as interpreted and applied in India wherever these two statutes have failed to make any provision. It may, however, be noted that even these two statutes have been framed on the basis of the English Common Law. So far as the second branch of the law on the subject is concerned Banking Companies incorporated in India are governed by the Indian Companies Act 1913 as amended by the Indian Companies (Amendment) Act of 1936 and bankers who are partnership firms are governed by the general law of partnership as contained in the Partnership Act. Individual bankers are governed by no Specific Statute, apart from the general civil and criminal law. Under the Indian Companies Act, 1939, as amended by the Companies Amendment Act of 1936, a banking company must comply with the provisions contained therein applicable to all companies e.g. the provisions relating to incorporation, registration, the hold-

ing of general meetings, auditing of balance sheets and so on. It must also comply with certain special provisions prescribed for banking companies by the Companies Amendment Act of 1936, e.g., special requirements regarding Capital, Reserve Fund and Cash Reserve. Apart from this the Reserve Bank Act, 1934, has set up the Reserve Bank and also a number of Scheduled Banks with a view to better control the banking organisation and the money market of the country as a whole.

#### **Definition :**

The term 'Banker' does not lend itself to an easy definition. Neither the Contract Act nor the Negotiable Instruments Act define the term. The Negotiable Instruments Act<sup>1</sup> simply states that a banker includes also persons or a corporation or company acting as bankers. This is similar to the definition given in Halsbury's Laws of England<sup>2</sup> which is as follows :—"A bank is a corporation, partnership or individual carrying on the business of banking." These definitions make it clear that a banker is distinguished by his function and business but do not define what that function and business is. Hart<sup>3</sup> defines a banker or a bank as a person or company carrying on the business of receiving monies and collecting drafts for customers, subject to the obligation of honouring cheques drawn on him by the customers to the extent of the amounts available in their current accounts. But this definition of Hart ignores the following facts, namely, (a) the customers may draw cheques not only on their current accounts but may draw on other accounts e.g., savings bank accounts; (b) the withdrawals of money by customers need not be by cheque alone; and (c) a banker combines other incidental businesses e.g., lending money to others, discounting bills of exchange and drafts and so on with a view to making profit. The Indian Companies Amendment Act of 1936<sup>4</sup> adopts a more exhaustive definition and defines a "Banking Company" as a company which carries on as its principal business the accepting of deposits of money on current account or otherwise, subject to withdrawal by cheque, draft or order, notwithstanding that it engages

<sup>1</sup> Sec. 3.

<sup>2</sup> Vol. I, page 568, Art. 1147.

<sup>3</sup> Hart on Banking, 4th ed.

<sup>4</sup> Sec. 277F.

addition in any one or more of the business mentioned in S. 277 F of the Act, which are more or less incidental to the business of banking. This we may also adopt as a satisfactory definition for all other banking concerns which are not companies by substituting the word "Concern" for "Company" wherever the latter occurs in the definition. It should be noted, however, that for the purposes of the Indian Companies Act, a company will be deemed to be banking company if it uses the word "Bank," or "Banking" as part of its name<sup>1</sup> and the liabilities imposed by that Act on Indian Companies will automatically attach to such company whether it actually carries on the business of banking or not. But for other purposes e.g., in matters relating to the payment or collection of cheques a concern will not have the rights and liabilities of a banker unless it trades or traffics in money, receives or remits money and negotiates bills of exchange etc., with a view to making a profit by such business<sup>2</sup>. Thus a stock broker and notary public, who largely engaged in trade, received money from some of his customers and paid it out again, and occasionally discounted drafts, but who neither held himself out as a banker, nor appeared to have been so considered is not a banker.<sup>3</sup> Similarly a trading concern dealing in cotton and opium cannot properly be called a banking business though they might have done a small amount of banking business by way of receiving money and advancing the same to others.<sup>4</sup> Nor can a Government treasury be regarded as a bank though local boards deposit money in it and the treasury pays out money according to their orders; for the element of making profit is absent.<sup>1</sup>

#### **Relation between A Banker and his Customer :**

The business of banker includes the receipt of money for and on behalf of the customer which constitutes him merely the debtor of the customer with the obligation to honour the cheques of the customer so long as there are enough funds in his hands<sup>2</sup>. As to who is a customer we shall discuss in detail later on under the heading collection of cheques. It is sufficient to note here

<sup>1</sup> Indian Companies Amendment Art. (XXI) of 1942

<sup>2</sup> Rangswami *vs.* Sankari, I.L.R. 43 Mad. 816.

<sup>3</sup> Stafford *vs.* Harry, 12 Ir. Eq. R. 400.

<sup>4</sup> The New Flemming Spinning & Weaving Co. *vs.* V. Kessowji. 9 n. 573, 411.

that a person may be regarded as the customer of a bank if he has some sort of account, either a deposit or a current account or some similar relation with the bank.<sup>1</sup> The principal duties of a bank *vis-a-vis* its customer are twofold, namely, (a) to pay the cheques drawn by the customer and (b) to collect cheques and drafts paid in by the customer. These are such important duties and may involve a bank in such heavy liabilities to the customer and also to third parties that we shall have to study these in detail. Apart from these a bank is not a trustee for the customer and the latter has no right to inquire into or question the use made of the money by the bank.<sup>2</sup> But the right of the bank to use its customers' money is subject to any specific appropriation which the customer may make in respect of the money paid by him e.g., where he pays money to reduce an overdraft account or to any particular account.

#### **Payment of Cheques :**

The obligation of a bank to pay the cheques of its customers is imposed in India by the Negotiable Instruments Act<sup>3</sup> which lays down that the drawee of a cheque (which in every case must be a bank) having sufficient funds of the drawer in his hands, properly applicable to the payment of such cheque must pay the cheque when duly required so to do, and, in default of such payment, must compensate the drawer for any loss or damage caused by such default. It follows from this that the bank is obliged to pay the cheque of its customer provided the following conditions are fulfilled, namely, (1) *there must be sufficient funds of the drawer* (2) *the funds must be properly applicable to the payment of the cheque*, (3) *the bank must be duly required to pay* and (4) *in default it must pay damages to the customer*. We shall discuss these conditions below.

(1) *Sufficient funds*--A bank is liable to pay the cheque of its customer only if there are sufficient funds to meet the cheque in its hands. If the cheque is for a larger amount than the funds of the customer in the hands of the bank, the bank is entitled to refuse payment. But where there is a contract between the bank

<sup>1</sup> Per Lord Davey in Great Western Railway Co. *vs.* London & County Banking Co., (1901) A.C. 414 at p. 420.

<sup>2</sup> *Foley vs. Hill*, (1848) 2 H.L. 28.

<sup>3</sup> Sec. 31.

and the customer to pay the cheque even in the absence of sufficient funds as when the bank agrees to allow overdraft facilities upto a certain limit, the bank will be liable for damages to the customer for breach of contract if it dishonours any cheque drawn by the customer for an amount not exceeding the overdraft limit.<sup>1</sup> A bank, however, is not liable to honour the cheques of a customer on his overdraft account where the bank has duly terminated the overdraft arrangement by notice to the customer.<sup>2</sup> A customer having an account with a particular branch of a bank cannot draw cheques on another branch of the same bank where he has no account and the latter is justified in refusing to honour his cheques.<sup>3</sup> It should be noted that the liability of a bank to honour the cheques of a customer does not depend on the sufficiency of the funds of the customer alone but also on its availability. A customer cannot draw against the amount covered by a cheque or draft drawn in his favour immediately after he has paid the same in for collection. The bank is entitled to a reasonable time for clearing or collecting cheques or drafts according to their respective nature.<sup>4</sup> Even in the case of notes or gold or a cheque upon itself, the bank is entitled to a reasonable time between the paying in and drawing against in which to carry out the necessary book-keeping entries.<sup>5</sup> If, however, the amount covered by a cheque or other instrument is credited as such by the bank as soon as the customer pays in, the customer is at once entitled to draw against it whether the bank has received the amount or not.<sup>6</sup>

(2) *Funds properly applicable*—This means that the payment required by a cheque must not be contrary to any contract subject to which the funds against which the cheque has been drawn are maintained or contrary to the purpose for which the account has been opened and kept. Thus if a customer opens an account with a bank subject to the condition and on the understanding that he will be entitled to draw only one cheque per week, the

<sup>1</sup> Fleming *vs.* Bank of New Zealand, (1900) A.C. 577.

<sup>2</sup> Roe *vs.* Bradford Banking Co., (1894) A.C. 586, 590.

<sup>3</sup> Woodland *vs.* Fear, (1857) 7 E. & B. 518.

<sup>4</sup> Whitaker *vs.* Bank of England, (1835) 1 Cr. M. & Rr. 744; Farman *vs.* Bank of England, (1902) 18 T.L.R. 339.

<sup>5</sup> Marzetti *vs.* Williams, (1830) 1 B. & Ad. 415.

<sup>6</sup> Capital & Counties Bank *vs.* Gordon, (1903) A.C. 240.

bank will have the right to refuse payment of any cheque drawn by the customer after the first cheque within the same week.

Similarly if an account is opened by a trustee, the bank has express notice that the funds are trust funds and it should refuse to honour a cheque drawn by the trustee in his favour or for some purpose other than the trust; for otherwise the bank will be liable for damage for conversion of trust moneys.<sup>1</sup> Similarly if an agent operating on the account of his principal draws a cheque on the account in his favour or in favour of his firm, the bank should refuse payment.<sup>2</sup> The last two illustrations are instances where payment by the bank would be contrary to the purpose of the account. As the question of trust accounts or moneys is a very difficult question we shall study it separately.

(3) *Duly Required to pay* :—The order to pay contained in a cheque must be made and communicated according to law and according to accepted practice and usage of the banking business. Thus a cheque must be presented to the bank within a reasonable time and a bank may refuse to pay a stale cheque.<sup>3</sup> Similarly the bank is not liable if the cheque is not presented within the banking hours or when it is not legal or is drawn in a form whose legality is doubtful,<sup>4</sup> or when it is irregular as when it is undated or post dated or contains unsigned alterations.

(4) *Payment of damages in Default* :—The liability of a bank which dishonours its customer's cheque without justification is liable to the customer only who draws the cheque. The holder or payee of the cheque has no right to enforce payment or claim damages from the bank unless the bank has admitted to him that it holds money specially to meet the particular cheque or has contracted with the holder or payee to honour the cheque, as in the case of irrevocable letters of credit opened by a bank in favour of the holder at the instance of a customer. The remedy of the holder is against the drawer in case of dishonour of the cheque. The reason is that the drawing of a cheque does not automatically operate as an assignment of money in the hands of the banker in favour of the payee. A customer who is aggrieved

<sup>1</sup> Plunkett *vs.* Barclays Bank, (1936) A.E.R. 653.

<sup>2</sup> British American Elevator Co. Ltd. *vs.* Bank of Br. N. America (1919) A.C. 658.

<sup>3</sup> S. 74 of the Negotiable Instruments Act.

<sup>4</sup> Hart on Banking, 4th ed 325.

by the wrongful dishonour of his cheque, may sue the bank on any one of the following three grounds :—

- (a) *Breach of Contract* :—The opening of an account by a customer with a bank creates an implied contract between the bank and the customer whereby the bank is obliged to honour the cheques of the customer provided the conditions mentioned above are fulfilled. If the bank dishonours the cheque of the customer without justification it commits breach of contract for which the customer is entitled to recover damages from the bank ;
- (b) *Negligence* : A bank has the duty of honouring cheques of its customer because of the implied contract subsisting between the two. Hence if the bank wrongfully dishonours the cheque of its customers it will amount to a breach of duty and the customer is entitled to sue the bank in tort instead of in contract for negligence and recover damages for injury to his credit and reputation
- (c) *Libel* :—A customer who is aggrieved by the wrongful dishonour of his cheque may base his action against the bank on libel where the bank dishonours his cheque with remarks like 'Refer to drawer' or 'Not covered' or 'Exceeds instruction' which is likely to convey the impression in the mind of the payee that he is a dishonest person who has obtained credit or value for cheques without being able to meet them<sup>1</sup>.

#### Measure of Damages :

According to the old decisions substantial damages were presumed to have been occasioned to a customer by the wrongful dishonour of his cheque and he was entitled to recover substantial damages even in the absence of actual proof of injury<sup>2</sup>. As Lord Tenterden observed in *Marzetti vs. Williams*<sup>3</sup>, "it is a discredit to a person and, therefore, injurious in fact, to have a draft refused

<sup>1</sup> *Lionell Barber & Co. vs. Deutsche Bank (Berlin) London Agency*, (1919) A.C. 304.

<sup>2</sup> *Rodin vs. Steward*, (1854) 14 C.B. 595; *Summers vs. City Bank*, (1874) L.R. 9 C.P. 580.

<sup>3</sup> (1830) 1 R. & Ad. 415.

payment for a small sum, for, it shows that the bank had very little confidence in the customer; it is particularly injurious to a person in trade." But the recent decisions have made a departure from the old law and seem to lay down that excepting where the customer is engaged in trade or business, actual proof of injury to credit must be given in order to entitle the aggrieved customer to recover substantial damages<sup>1</sup>. It seems that professional men will be regarded as in the same category as business people and will be entitled to recover substantial damages without actual proof of injury if their cheques are wrongfully dishonoured. For why should not the professional honour and credit of a solicitor or doctor be regarded as damaged and his prospects injured by dishonour of a cheque in the same way as that of a green grocer or a butcher?

#### **Discharge of the Bank's Liability :**

Where a cheque payable to order purports to be endorsed by or on behalf of the drawee is discharged by payment in due course.<sup>2</sup> Where a cheque is originally expressed to be payable to bearer, the drawee is discharged by payment in due course to the bearer thereof, notwithstanding any endorsement whether in full or in blank appearing thereon, and notwithstanding that any such endorsement purports to restrict or exclude further negotiation<sup>3</sup>. 'Payment in due course' means payment in accordance with the apparent tenor of the instrument in good faith and without negligence to any person in possession thereof under circumstances which do not afford a reasonable ground for believing that he is not entitled to receive payment of the amount therein mentioned.<sup>4</sup> Apparent tenor of an instrument means what appears to be the intention of the parties on the face of the instrument. Thus if a cheque is drawn payable to A or order the apparent tenor is that the payment should be made either to A or his endorsee. If the cheque bears an endorsement of A in blank the cheque becomes payable to bearer. If the cheque bears an endorsement of A in favour of B the cheque becomes payable to B. The bank will be relieved from liability if it pays the amount of the cheque

<sup>1</sup> Wilson *vs.* United Counties Bank, (1920) A.C. 102, 112.

<sup>2</sup> Negotiable Instruments Act, S. 85 (1).

<sup>3</sup> Ibid, S. 85 (2).

<sup>4</sup> Negotiable Instruments Act, S. 10.

to the bearer in one case and to B in the other provided there was nothing irregular or suspicious in the endorsement of A which would make the bank doubt that the holder is not entitled to receive payment.

#### Bearer Cheques :

A banker who in good faith and without negligence i.e., in due course pays a discharged bearer cheque to the person who presents it is discharged from all liability and can debit his customer though the holder had no title or a defective title e.g., when he stole the cheque or found it after it was lost.<sup>1</sup> But a payment before the due date<sup>2</sup> or the payment of a cancelled cheque in circumstances such as to excite suspicion<sup>3</sup> cannot be regarded as payment in due course and the bank will remain liable for the amount of the cheque to the customer even after such payment. So also where the payee of a certain cheque sent his servant for cashing the cheque and the officials of the bank through mistake or inadvertence paid the amount to a wrong person after taking the cheque from the servant, it was held that the bank must pay over the money again to the payee.<sup>4</sup> A bearer cheque does not cease to be a bearer cheque even if there are subsequent endorsements on it and even if any of these endorsements purport to make it an order cheque or a non-negotiable one.<sup>5</sup> But if a bearer cheque is crossed the bank cannot pay it over the counter in disregard of the crossing. The bank must not pay it except through another bank and if it does it cannot debit its customer with the amount of the cheque.<sup>6</sup>

#### Order Cheques :

As regards order cheques the bank is discharged if it pays to the payee or to his endorsee. But the difficulty arises where the endorsement is forged and the payment is made by the bank to the indorsee of such forged endorsement. If the bank pays in

<sup>1</sup> Hellamy *vs.* Marjoribanks, (1852) 7 Ex. 389; Charles *vs.* Blackwell, (1877) 2 C.P.D. 151.

<sup>2</sup> Morley *vs.* Culverwell, (1840) 7 M. & W. 174.

<sup>3</sup> Scholey *vs.* Ramabottom, (1810) 2 Camp. 485

<sup>4</sup> Lall Chand *vs.* Agra Bank, 18 I.A. 111.

<sup>5</sup> Negotiable Instruments Act, S. 85 (2).

<sup>6</sup> Smith *vs.* Union Bank of London, (1875) 1 Q.B.D. 31, 35; Charles *vs.* Blackwell, *supra*.

good faith and without negligence *i.e.*, in due course the bank will not be liable. But if the bank is negligent *i.e.*, makes payment not in due course it cannot debit the customer with the amount of the cheque. What is negligence and whether a payment is in due course or not is a question of fact to be determined by the circumstances of each case. But the following may be cited as instances where a bank has been held to be negligent in the matter of payment :—

- (a) Where a bank pays a cheque in spite of patent irregularity in the endorsement. An endorsement is regarded as irregular where it does not correspond to the name as written and spelt in the body of the instrument. Thus if a cheque is drawn in favour of a person spelt as "John Robert Williams" or order it will be an irregular endorsement if the payee endorses it as J. R. Williams or J. Williams. In *Slingsby vs. District Bank*<sup>1</sup> a cheque was originally drawn "Pay J. P. & Co. or order" having a space between 'Co.' and 'or.' The cheque was got hold of by a fraudulent person who altered the cheque as payable to "J. P. & Co., per C. & P. or order" by inserting per C. & P. in the space between "Co" and "or." He then endorsed on the back of the cheque by putting C. & P. only and obtained payment from the bank. It was held that apart from the question of alteration the endorsement was irregular without the name of J. P. & Co., and the bank was guilty of negligence in making payment on such endorsement and was not entitled to protection.
- (b) Where bank pays a cheque inspite of unauthorised alterations *e.g.*, where the alteration is not initialled by the drawer or initialled by some only and not all the drawers in case there are more than one drawer.<sup>2</sup>
- (c) Where a bank pays a cheque contrary to directions given regarding the disposal of the money payable under the cheque. Thus where by arrangement between a company and its bank, the cheques of the company were to be paid in the form of bank-drafts issued by the bank in favour

<sup>1</sup> (1932) 1 K.B. 544.

<sup>2</sup> *Kepitigulla Rubber Estates Ltd. vs. National Bank of India*, (1909) 2 K.B. 1010

of foreign constituents of the company for the amounts of the cheques and the bank in a few cases issued bank drafts in the name of the manager of the company without taking due care and being misled by the fraud of the manager and the proceeds whereof were misappropriated by the manager, it was held that the bank was negligent in not complying with the directions of the company and was not entitled to debit the company with the amounts of the drafts issued in the name of the manager.<sup>1</sup>

- (d) Where a bank pays a cheque after countermand i.e., after the customer stops payment and the countermand is communicated to the bank.<sup>2</sup>
- (e) Where a bank pays before the due date.<sup>3</sup>
- (f) Where a bank pays a crossed cheque which has been opened by writing "pay cash" and initialled. In such case the bank pays such a cheque at its own risk and will be liable for the amount paid in case the opening proves unauthorised.
- (g) Where a bank pays a cheque on which the customer's name has been forged. Such a cheque is no cheque<sup>4</sup> and it has been held that a bank ought to know its customer's signature.<sup>5</sup>

#### Determination of the Duty and Authority to Pay :

The duty and authority of a bank to pay a cheque drawn by a customer are determined :—

- (1) By countermand of payment commonly known as stopping a cheque. In England this is provided for by S. 75 of the Bills of Exchange Act, 1882. In India there is no similar provision in the Negotiable Instruments Act. But it is submitted that the law is the same in India as in England ; for a payment after countermand would not be a payment in due course<sup>6</sup> and generally

<sup>1</sup> Bank of Montreal *vs.* Dominion Gresham Guarante Co., (1930) A.C. 559.

<sup>2</sup> Justice *vs.* London City and Midland Bank, (1908) 1 K.B. 293.

<sup>3</sup> Morley *vs.* Culverwell, (1840) 7 M. & W. 174.

<sup>4</sup> Imperial Bank of Canada *vs.* Bank of Hamilton, (1903) A.C. 49.

<sup>5</sup> Holmes *vs.* Blackett, (1877) 2 C.P.D. 157.

<sup>6</sup> Imperial *vs.* Sadler, I.L.R. (1873) Nag. 587.

a customer<sup>1</sup> who has the right to require the bank to pay has the right to revoke that order.<sup>2</sup> A countermand to be effective must be communicated to the bank.<sup>3</sup> But a bank is not bound to stop payment of a cheque simply on the basis of an unauthenticated telegram.<sup>4</sup> A Bank which, however, stops payment by acting reasonably on the receipt of a telegram countermanding payment cannot be held liable for damages for wrongful dishonour if the telegram turns out to be unauthorised.<sup>5</sup> A countermand should also be free from ambiguity and if it is ambiguous the bank is entitled to pay the cheque. Thus in *Westminister Bank vs. Hilton*<sup>6</sup> a customer telegrammed and also telephoned to the Bank to stop payment of cheque No. 117283 for £8/- and odd to the payee Pote. A cheque bearing No. 117285 and for the same sum payable to Pote and bearing a date subsequent to the date of the countermand was presented and paid by the bank. It was held by the House of Lords that as the No. of the cheque paid was different to the number mentioned in the countermand and as the cheque bore a date subsequent to the date of the countermand the bank was justified in thinking that the cheque might have been a duplicate one and it was bound to cash it. It was observed : "It must be remembered that a bank would be sued just as much for failing to honour a cheque as for cashing one which had been stopped, and that the number of the cheque was one item of identification." The right to countermand is only exercisable by the drawer. If a cheque payable to bearer is lost the holder should ask the drawer to countermand. But if a cheque is payable to order and hence requires endorsement before payment, the holder may, in case it is lost, inform the bank directly about the loss and the bank should not pay the cheque, as otherwise, it will not be a payment in due course. One partner has the power to stop a cheque issued in the firm's name; one executor can stop payment of a cheque signed by another; and one of two or more customers on a joint account can stop the cheque issued against the account.<sup>7</sup>

(2) *By notice of the customers' death*—This is also provided.

<sup>1</sup> *Syed Mahomed vs. Emperial Bank*, (1940) 2 Cal. 578.

<sup>2</sup> *Curtice vs. London City and Midland Bank*, (1908) 1 K.B. 293.

<sup>3</sup> *Ibid.*

<sup>4</sup> *Lalla Mal vs. Kesho Das*, 29 All. 49.

<sup>5</sup> (1926) 136 L.T. 314 (H.L.).

<sup>6</sup> *Grant vs. Taylor*, (1843), 2 Hare 413.

for in England by S. 75 of the Bills of Exchange Act, 1882. But in India there is no such specific provision and the question falls to be determined by the general law. On the death of a customer his funds in the bank vest in his legal representative and any cheque issued by him and not cashed before his death cannot be cashed thereafter. For his own order cannot operate to withdraw any part of the Funds which have already vested in his legal representative. But if the bank pays his cheque before it has had notice of his death, the payment is valid.<sup>1</sup> Where one of two or more customers or partners on a joint account dies the survivors or survivor can still draw on the account. But it is preferable that, where to the knowledge of the banker a partner dies, the old account should be operated only for the purpose of winding up the partnership and arrangements should be made for a new account, carrying over to it any balance remaining<sup>2</sup>.

In the case of death of one of two or more trustees, however, the bank must not honour cheques on the trust account drawn by the survivor or survivors unless it is satisfied that such survivor or survivors have the power so to draw under the terms of the trust.

(3) *By the customer's insolvency or where the customer is a company, by the liquidation of the company* :—On receiving notice of an order of adjudication or the presentation of a petition for adjudication of the customer or of any act of insolvency committed by the customer, the bank should stop payment of all cheques issued by the customer. The reason is that under the Presidency Towns Insolvency Act, insolvency commences from the date of the earliest Act of Insolvency and under the Provincial Insolvency Act, it commences from the date of the presentation of the petition. In the case of insolvency under the Presidency Towns Insolvency Act, therefore, a bank will not be justified in paying cheques issued by a customer after the bank has notice of any act of insolvency committed by the customer.

If it does the official assignee can claim back the money so paid since the official assignee is entitled to all the property of the insolvent as from the date of insolvency. In the case of insolvency under the Provincial Insolvency Act, a bank will not be justified

<sup>1</sup> Roger *vs.* Ladbrooke, (1822) 1 Bing. 93 ; In Re Beaumont, (1902) 1 Ch. 889, 894.

<sup>2</sup> Re Bourne, (1906) 2 Ch. 427.

in paying the cheque of a customer after it has notice that a petition for adjudicating the customer insolvent has been presented. Where the customer is a company all the property of the company will vest in the liquidator, in case the company is wound up, as from the date of the order for winding up. Hence the bank should not pay the cheques of the company after it has notice of the winding-up order.

(4) *By notice of the customer's lunacy*—Where a customer is adjudged a lunatic by a competent court, the bank must stop payment of all cheques issued by the lunatic from the date on which the bank receives notice of the order of the court<sup>1</sup>.

(5) *By service of a garnishee order or attachment or injunction in respect of the funds of the customer*—A garnishee order is an order made against a third party with whom a defendant against whom a decree has been passed has money or other property requiring him to pay over the money or the property to court. A garnishee order against the bank is generally made in the following manner. The money belonging to the customer is attached first. Then the decree holder makes an application before the court which has ordered the attachment for an order against the bank to pay the attached money to court. The notice or summons of the application is then served on the bank requiring it to show cause why the order should not be made against it. Where the bank has any reason to oppose the order e.g., where it claims a lien over the money or where it states that it has not got any money belonging to the customer, it appears before the court and opposes and if the court is satisfied that the bank's objection is justified it will not make any order. If the bank shows no cause an order is made in due course. An attachment is effected by serving the bank with a prohibitory order forbidding it to deal with the money attached without further orders.<sup>2</sup> Sometime the court before which a suit has been instituted against the customer may pass an injunction against the customer restraining him from withdrawing the money lying with the bank. In all cases where there has been a garnishee order or attachment against the bank or an injunction passed

<sup>1</sup> *Dow v. Nuan*, (1879) 4 Q.B.D. 661; *Daily Telegraph Newspaper Co. Ltd. v. Longlin*, (1904) A.C. 776.

<sup>2</sup> Chap. XVIII, r. 1 of the Calcutta High Court Original Side Rules.

against the customer and the bank has notice of it, the bank must stop paying the customer's cheque and the bank cannot even pay a cheque drawn prior to such order.<sup>1</sup> In the case of a garnishee attachment the bank will be liable to pay over again to the creditor of the customer if it pays out the attached money to the customer in violation of the garnishee attachment.<sup>2</sup> But only those funds of the customer, which have become due or are accruing due at a definite and certain approaching date, can be attached by way of a garnishee order.<sup>3</sup> Hence an amount paid in by the customer subsequent to the garnishee attachment for which a new account was opened is not affected by the attachment.<sup>4</sup> The following sums are not attachable by way of garnishee : (a) a deposit account repayable only on production of the receipt (b) a deposit account repayable on fixed notice which has not been given.<sup>5</sup> The following are attachable : (a) a current account, (b) a deposit account repayable on demand, (c) a deposit account repayable on fixed notice which has been given, (d) a deposit account repayable at a fixed future date or after the lapse of a specified time.<sup>6</sup>

(6) Where notice has been given either by the customer or the bank closing the account of the customer. In the absence of any agreement either the customer or the bank can close an account by notice to the other. But a bank is not entitled to close an account and dishonour cheques drawn on it without having given a reasonable notice to the customer.<sup>7</sup> A bank may, however, at the time of the opening of an account stipulate that it can close the account at any time without notice to the customer and such a stipulation is not invalid.<sup>8</sup>

(7) Where the bank has been notified by its customer about the loss of a cheque.

<sup>1</sup> *Robert vs. Whitley*, (1842) A.C. 118

<sup>2</sup> *Edmunds vs. Edmunds*, (1904) P. 362.

<sup>3</sup> *Jones vs. Thompson*, (1858) 27 L.J.Q.B. 234

<sup>4</sup> *Heppinstall vs. Jackson*, (1939) 2 A.E.R. 10

<sup>5</sup> *Halsbury's Law of England*, Vol I, p. 588.

<sup>6</sup> *Ibid*

<sup>7</sup> *Buckingham & Co. vs. London Midland Bank*, (1895) 12 L.T.R. 70 ; *Agra and Masterman's Bank Ltd vs. Hoffman*, (1864) 34 L.J. Ch. 285 ; *Thomas vs. Howell*, (1874) L.R. 18 Eq. 198 ; *Perry vs. Halifax Commercial Banking Co.*, (1901) 1 Ch. 188.

<sup>8</sup> *Champion Automobile Ltd. vs. T. N. and Q. Bank*, (1938) Mad. 77.

**Accounts :**

In the matter of opening accounts for customers a bank usually insists on certain formalities being observed, for a banker incurs certain liabilities to its customer as well as to strangers in the matter of paying cheques or drafts for and on behalf of their customers. In the first instance the bank requires from a new customer, proposing to open an account, some form of introduction either by reference to some person known to the manager of the bank or to some other bank. The bank then makes confidential enquiries regarding the customer from such person or bank. If the bank is satisfied regarding the standing of the customer, the bank agrees to open the account. The next step is for the bank to obtain the specimen signature of the customer or any other person who is to operate on the account. Then the customer is given a cheque book containing a number of cheques which he will be entitled to use to draw on the account. He is also given a pass book and a book containing a number of 'paying-in-slips' (popularly known in India as the Challan book). All payments to be made by or on behalf of the customer whether by cash or cheque or otherwise should be entered into one of these paying-in-slips and signed by the customer or his agent and produced before the receiving cashier at the time of paying in. The receiving cashier stamps and initials the slip and the counterfoil and returns the counterfoil to the customer which serves as an acknowledgement of the receipt of the payment by the bank.

**Current Deposit and Savings Bank Account :**

A current account is one on which the customer can draw by cheque or otherwise as many times in the week as he likes. A savings bank account is one which usually stipulates that the customer can draw on it by cheque only once a week. A deposit account is one in which the funds are usually kept for a fixed and long period and cannot be drawn against before it is due. A deposit account is usually of the following varieties : (a) A deposit account repayable only on production of the receipt in which case the money is not due until the production of the receipt, (b) a deposit account repayable on fixed notice in which case the money is not due until a notice has been given and the notice expires, (c) a deposit account repayable at a fixed future date, or after the lapse of a specified time in which case the money is not due until after the arrival of the fixed date or the lapse of

the specified time. It is doubtful whether cheques can be drawn even against a deposit account repayable on demand<sup>1</sup>. The view expressed by Mallins *v.* C. in favour of the validity of such cheques in *Hopkins v. Abbott*<sup>2</sup> and *Stein v. Ritherdon*<sup>3</sup> does not seem to be sound<sup>4</sup>. A bank generally pays a certain rate of interest on moneys lying in savings Bank and Deposit Account but pays no interest on current deposit.

### **Joint Account :**

When an account is opened in the name of two or more persons jointly, it is called a joint account. In the absence of any agreement cheques drawn on an ordinary joint account should be signed by all the parties in whose name the account stands.<sup>5</sup> But by agreement the parties may stipulate that any one of them may draw on the joint account without the concurrence or signature of the other.<sup>6</sup> In case of death of any one of the parties, the bank is justified in allowing the survivor to draw any balance standing to the joint account, even as between husband and wife, whether both or either one is entitled to draw.<sup>7</sup>

### **Partnership Account :**

Where account is opened in the name of a partnership firm, it is known as partnership account. All cheques on the account must be drawn in the name of the firm and in the absence of instruction to the contrary every partner has the right to draw on the partnership account in the name of the firm<sup>8</sup>. The very fact that an account has been opened in the firm's name is evidence of authority of each partner to draw.<sup>9</sup> In the case of death of one or more partners the surviving partner or partners may draw on the firm account.<sup>10</sup> But the modern practice is that on the

<sup>1</sup> *Re Head* (No. 1), (1894) 2 Ch. 237

<sup>2</sup> (1875) L.R. 19 Eq. 222 at p. 223.

<sup>3</sup> 37 L.J. Ch. 369.

<sup>4</sup> *Halsbury's Laws of England*, Vol. I, 588 at p. 589.

<sup>5</sup> *Husband v. Davis*, (1851) 10 C.B. 645.

<sup>6</sup> *Marshall v. Cutwell*, (1875) L.R. 20 Eq. 328.

<sup>7</sup> *Halsbury's Laws of England*, Vol. I, 504.

<sup>8</sup> *Twihull v. London Suburban Bank*, (1869) W.N. 127.

<sup>9</sup> *Halsbury's Laws of England*, Vol. I, 604 under footnote (n); Indian Partnership Act, S. 12.

<sup>10</sup> *Backhouse v. Charlton*, (1878), 8 Ch.D. 444.

death of a partner, the partnership account should be operated on only for the purpose of winding up the partnership and the bank should insist on opening a new account with the balance, if any, remaining of the old account.<sup>1</sup>

#### Accounts of Companies and Corporations :

Where a company opens an account, the bank should ascertain as to who is authorised to draw cheques on the account under the Articles and Memorandum of the Company. Usually at the time of opening the account the bank satisfies itself as to the persons entitled to draw on the account and obtain their specimen signatures. The bank is only obliged to look into the articles and memorandum of the Company in order to find out the scope and authority of the persons dealing with the Company's account. It is not bound to enquire into the regularity of the proceedings what Lord Hatherly called the 'indoor management of the company'.<sup>2</sup> If a director has the authority under articles and memorandum of the company to draw cheques on the company's account, the bank will honour cheques drawn by him and the bank will not be liable to the company if it turns out that the cheque was in fact issued for a purpose other than that of the company or that the board of directors had by a resolution limited his authority to draw cheques, unless the bank has notice, express or implied, of the same.<sup>3</sup> But the bank must scrupulously comply with the directions given at the time of the opening of the account. Thus if the cheques on a company's account are to be drawn by at least two directors, according to the directions given, and the bank negligently and contrary to directions pays cheques signed by one of them only or signed by a new director who has no authority to draw and as to whose authority the bank makes no enquiry, the bank would be liable to the company for the amount of the cheque unless the same is paid to the creditors of the company.<sup>4</sup> In such a case the bank would pay the cheques at its own risk and should the cheques be drawn in favour of persons who are not the creditors of the

<sup>1</sup> Halsbury's Laws of England, Vol. I, 604 at p. 605.

<sup>2</sup> Royal British Bank *vs.* Turquand, (1856) 6 E. & B. 327.

<sup>3</sup> Houghton & Co. *vs.* Nothard Lowe & Wills Ltd., (1928) A.C. 1 Underwood Ltd. *vs.* Bank of Liverpool, (1924) 1 K.B. 775.

<sup>4</sup> Liggett *vs.* Barclay's Bank, (1928) 1 K.B. 46.

company, the bank would be liable for the amount of the cheques. A payment contrary to directions is also illustrated by the case of *Bank of Montreal v. Dominion Gresham Guarantee Co.*,<sup>1</sup> which we have discussed before<sup>2</sup>.

#### Trust Account :

A trust account is constituted where a trustee or trustees open an account expressly as trustees and also where the trustee opens an account in his personal name but the bank is fixed with notice of the trust either by the very nature of the account or by express notice thereof<sup>3</sup>. A trust account is one in which the person or persons entitled to the benefits thereof is or are not the person or persons in whom the legal title of the account vests. Thus if A transfers Rs. 50,000/- to B in trust for a village school, the legal title of the sum of Rs. 50,000/- will vest in B who is the trustee and the party who is entitled to the benefits of the money is the school which is called the beneficiary or the "cestui que trust". A trustee cannot use the trust money for his own benefit for any purpose other than that of the trust. Hence if an account is opened by a trustee as a trustee, the bank has express notice that the funds are trust funds, and it should refuse to honour cheques by the trustee in his own favour or for any purpose alien to the trust if that is obvious; otherwise it will be liable for conversion to the beneficiaries<sup>4</sup>. But difficulties arise where the trustee opens the account not as a trustee expressly. In such a case a trust is implied if the trust is obvious from the nature of the account e.g., where the account is headed "Police Account," or "School Account."<sup>5</sup> But an account headed "Office Account"<sup>6</sup> has been held not to imply any trust, for a man may divide his account into personal and office accounts<sup>7</sup>. If the money belonging to a trust account is drawn out and paid into the private account of the trustee the bank is liable to make good the money so drawn out.<sup>8</sup> A bank may also be held liable for wrongfully

<sup>1</sup> (1930) A.C. 659

<sup>2</sup> See *supra*.

<sup>3</sup> *Plumkett v. Barclay's Bank*, (1936) A.E.R. 653.

<sup>4</sup> *Ibid.*

<sup>5</sup> *Ex parte Kingston*, (1871) L.R. 6 Ch. App. 631.

<sup>6</sup> *Greenwood Teale v. Williams Brown & Co.*, (1894) 11 T.L.R. 56.

<sup>7</sup> *Re West London Commercial Bank*, (1838) 58 Ch. 364.

paying out trust moneys if it receives independent intimation regarding the trust where the trust is not obvious or the account is not an express trust account,<sup>1</sup> and a bank cannot obtain protection by wilfully refraining from obtaining information as to the trust character of the account.<sup>2</sup> But the bank is under no duty to scrutinise the purpose of every cheque drawn by a trustee and if it is otherwise regular it is bound to honour such cheque and it is not to be held liable for such payment.<sup>3</sup> The bank is entitled to presume that the act of a trustee in drawing cheques for third parties is in the course of the lawful performance of his duty and honour such cheques accordingly.<sup>4</sup>

Where there are more than one trustee, all the trustees must jointly sign a cheque drawn on the trust account unless the terms of the trust provide otherwise and on the death of one of several trustees the bank must not honour cheques on the trust account drawn by the survivor or survivors unless otherwise provided by the terms of the trust.

#### Executor's and Administrator's Account :

Where an account is opened by the executor or administrator of a deceased person in respect of funds belonging to the estate of the deceased, such an account is called the executor's account or the administrator's account as the case may be. A bank must not honour cheques drawn by an executor or administrator for his own benefit or for purposes other than that of paying the debts and legacies of the deceased provided the bank has express or implied notice of the same. In this respect the liability of the bank is similar to that in relation to trust account. Where there are more than one executor or administrator, each can separately operate and draw cheques on the account unless they are forbidden to do so by the will of the deceased or the letters of administration.<sup>5</sup> Hence on the death of one of several executors or administrators, the bank may pay cheques drawn by the survivor or survivors and such a payment will exonerate the bank.<sup>6</sup>

<sup>1</sup> Bodenham *vs.* Hopkins, (1842) 21 L.J. Ch. 864.

<sup>2</sup> London & Stock Bank *vs.* Simmons, (1892) A.C. 201.

<sup>3</sup> Thompson *vs.* Clydesdale Bank Ltd., (1893) A.C. 282.

<sup>4</sup> Coleman *vs.* Bucks & Oxon Union Bank, (1897) 2 Ch. 243.

<sup>5</sup> Ex parte Rigby, (1815) 19 Ves. 463.

<sup>6</sup> Clough *vs.* Bond, (1846) 3 My. & Cr. 490.

### **Agent's Account :**

Where an agent operates an account on behalf of his principal to the knowledge of the bank, the bank must see that the agent acts within the scope of his authority and does not misuse his position. Thus where the customer of a bank who was the agent of a company and was, according to the terms of the agency, bound to use the proceeds of drafts drawn on the principal for the purpose of paying for the purchases made by him on his principal's behalf, discounted some of those drafts with the bank and paid the proceeds into his own account it was held the bank was liable for conversion and was bound to pay the proceeds of these drafts to the principal company.<sup>1</sup> So also where a person authorised under a power of attorney to draw cheques on the customer's account, drew and paid them into his own private account, the bank which paid and collected the cheques were held guilty of negligence and liable to pay the amount of the cheques to the customer since they had notice that the agent was using the principal's money for his own purpose.<sup>2</sup> Similarly where an agent authorised to operate on the principal's account for seeking more profitable investment used the funds to adjust his own debts to the bank, it was held that the bank was not entitled to debit the principal's account by such adjustment.<sup>3</sup>

### **Forged or Altered Cheques :**

A cheque purported to be drawn by the customer to which the customer's name as drawer has been forged is not a cheque, but a mere nullity.<sup>4</sup> A bank is supposed to know the signature of its customer and detect any imitation<sup>5</sup> and if it makes any payment on such a cheque it cannot debit the customer with the amount of payment unless it can establish estoppel or adoption on the part of the customer. The real ground for the banker's obligation in this respect is not, however, his supposed knowledge of the customer's signature but the fact of his having made payment

<sup>1</sup> British American Elevator Co. Ltd. *vs.* Bank of British North America, (1919) A.C. 658.

<sup>2</sup> Rickett *vs.* Barnett, (1929) A.C. 176; Lloyds Bank *vs.* Savory, (1933) A.C. 201, 229.

<sup>3</sup> Imperial Bank *vs.* Mary Victoria, (1936) P.C. 193.

<sup>4</sup> Imperial Bank of Canada *vs.* Bank of Hamilton, (1903) A.C. 49.

<sup>5</sup> Smith *vs.* Mercer, (1815) 6 Taunt, 76.

without the authority of the customer.<sup>1</sup> But if a man knows or has reasonable ground for believing, that his signature has been forged to a cheque, and that it is about to be presented to his bank for payment, he must warn the bank. If he fails to do so and the bank's position is thereby prejudiced, e.g., where the bank loses the opportunity of protecting itself against subsequent forgeries, if any, or the opportunity of taking proceedings, civil or criminal, against the forger as by his escaping out of the jurisdiction, he will be held to have adopted the cheque and estopped from denying that the signature is his own. Mere silence, however, of the customer without the bank's position being prejudiced as above does not create estoppel or constitute adoption.<sup>2</sup> Nor would it work estoppel if the customer consciously pays a cheque to which his name has been forged and disputes a subsequent forgery by the same person unless repetition of such payment establishes a course of business authorising the use of his name by the forger.<sup>3</sup>

As regards cheques originally issued and signed by the customer but which have been subsequently altered by forgery the position is different and there are conflicting decisions on the law. Material alterations may be of various kinds e.g. the amount may be altered or a crossing may be obliterated or an order cheque may be made into a bearer cheque. In India a bank paying a cheque which has been materially altered is absolutely protected under the following conditions: (1) where the alteration is not apparent or in the case of an alteration which takes the form of obliterating an original crossing and the original crossing is not apparent and (2) where the bank pay, according to the apparent tenor of the cheque. But where the alteration is apparent or noticeable on a reasonable scrutiny, the bank is liable for any loss suffered by the customer by such alteration unless there is a breach of any duty owed by the customer to the bank caused by the neglect of some usual or proper precaution.<sup>4</sup> The Privy Council recognised in

<sup>1</sup> London River Plate Bank v. Bank of Liverpool (1896) 1 Q.B. 7

<sup>2</sup> M'Kenzie v. British Linen Co., (1881) 6 A.C. 82

<sup>3</sup> M'Kenzie v. British Linen Co., (1881) 6 A.C. 82

<sup>4</sup> Morris v. Bethell, (1869), L.R. 5 C.P. 47

<sup>5</sup> Negotiable Instruments Act, S. 89

<sup>6</sup> Mercantile Bank of India v. Central Bank of India I.L.R. (1938) Mad. 370 P.C.)

Colonial Bank of Australasia *vs* Marshall<sup>1</sup> that the customer owes a duty to the bank but this duty has never been defined. In that case the Privy Council held that a customer is under no duty to fill up a cheque in such a way as would not facilitate forgery e.g., leaving spaces so that the forger can utilise it and overruled the old decisions Young *vs* Grote and Macussen *vs* Birkbeck Bank<sup>2</sup> which held a contrary view. But in *111* the decision by the House of Lords in London Joint Stock Bank *vs* Macmillan,<sup>3</sup> the old view in Young *vs* Grote has been affirmed and the decision of the Privy Council in the above case has been dissentient from and it has been held that a customer is bound to exercise reasonable care to prevent his banker from being misled and if in breach of such duty, he draws a cheque in a manner which facilitates fraud he is responsible for the loss and direct consequence of his act. The latest Privy Council decision in Mercantile Bank of India v. Central Bank of Ind<sup>4</sup> is not defined the duty of a drawer in drawing cheques as it was not a case of a cheque. But what it decides is that even where there is a duty owed by the drawer a mere breach of it will not exonerate the bank unless it is also proved that such a breach was the result of neglect or some usual or proper precaution. From this mass of conflicting decisions one thing is clear that so far as India is concerned 'the law as laid down by the Privy Council in the case of Colonial Bank of Australasia is still binding in spite of the decision of the House of Lords to the contrary in the above case until it is upset by another decision of the Privy Council. But the Privy Council recognises *v.n.* in this case that the customer owes a duty to the bank and it's submitted that such a duty consists in not doing something which would proximately and directly cause a loss to the bank. The duty is purely negative and the customer need not do anything positive to prevent e.g., a fraud tor, in the words of the Privy Council people are not supposed to commit forgery. Thus if a man draws a blank cheque and leaves it in a public place whence it is taken by a forger who fills up the cheque and cashes it, the bank will probably not be liable for the customer.

<sup>1</sup> (1906) A.C. 559 at 567

<sup>2</sup> (1827) 4 Bing. 253

<sup>3</sup> (1859) 5 T.L.R. 179, 463 and 646 (C.A.)

<sup>4</sup> (1918) A.C. 777

<sup>5</sup> L.L.R. (1938) Mad. 360 (P.C.).

did not do something which he was under a duty to do, namely not leaving a blank cheque in a public place without taking the usual and proper precaution against it being lost.

It should be noticed, however, that in any event where the alteration has the effect of increasing the amount paid, the bank can always charge the customer with the original amount and the dispute is, in every case, regarding the excess.<sup>1</sup>

#### **Payment of Drafts :**

A banker's draft is an order addressed by one bank to another or by one office of a bank to another office of the same bank to pay a specified sum to the payee named in his order. But a branch office of a bank cannot issue a draft payable to bearer on demand on the head office or another branch of the same bank and *vice versa*.<sup>2</sup> Hence drafts between two branches or a branch and head office of the same bank must be issued payable to the payee or order. Where any such draft drawn by one office of a bank upon another office of the same bank for a sum of money payable to order on demand, purports to be endorsed by or on behalf of the payee, the bank is discharged by payment in due course.<sup>3</sup> We have already explained what is implied by payment in due course and what would not amount to payment in due course. The bank will not be liable if it pays on a forged indorsement so long as the endorsement is regular and there is nothing to suggest any suspicion. Such drafts cannot be regarded as cheques since the drawer and the drawee are in law the same. Hence they cannot be crossed. But the protection against liability for payment on forged endorsements as indicated above makes hardly any difference for the bank as to whether they are crossed or not. Even if such a draft bears any crossing the bank must pay it across the counter on presentment provided it is duly endorsed.<sup>4</sup> If the bank refuses to pay the holder can sue the bank either as drawer of a bill or maker of a promissory note.<sup>5</sup>

Drafts drawn by one bank on another are to be regarded as cheques and the law relating to their payment by the drawee bank

<sup>1</sup> Imperial Bank of Canada *vs.* Hamilton, (1903) A.C. 49.

<sup>2</sup> S. 31 of the Reserve Bank of India Act.

<sup>3</sup> S. 65A of the Negotiable Instruments Act.

<sup>4</sup> Halsbury's Laws of England, Vol. I, pages 612, 613.

<sup>5</sup> *Ibid.*, p. 613.

is the same as in the case of cheques which we have discussed before. Such cheques may be crossed and if so they can be paid only when presented by a bank.

#### **Payment of Bills of Exchange Accepted Payable at a Banker's :**

"Where a customer accepts a bill payable at his banker's it constitutes an authority to the banker to pay it at maturity and if no funds are available, amounts to a request for an overdraft, the banker is under no obligation to pay the bill, even though he has sufficient funds in hand.<sup>1</sup> The bank can charge the amount of the bill on the customer if the bill is payable to bearer and the bank pays the bearer in due course. A bill of exchange is payable to bearer if it is stated to be so or endorsed in blank<sup>2</sup> or if the payee is fictitious. But if the acceptance of the customer is forged the bank cannot charge the customer with the amount of the bill on the same principle as that by which a customer cannot be charged with the amount of a cheque to which the customer's signature has been forged unless the customer is precluded from denying his signature by estoppel or adoption. We have already discussed the principle of estoppel and adoption. A bank is also not entitled to charge the amount of the bill on the customer if the bill is payable to order and payment has been obtained on forged endorsement of the payee's name even if the payment has been made in due course. S. 82 (1) of the Negotiable Instruments Act protects a bank only when it pays a bearer bill in due course and in the case of no other bills. Hence it is safe for a bank to insist on bills payable to order being presented through a bank for payment.

#### **Collection of Cheques :**

One of the principal duties of a bank is to collect cheques drawn on other banks and paid in by its customers for collection. While discharging this function it is known as a collecting bank as distinguished from a drawee bank on which the cheques are

<sup>1</sup> Halsbury's Laws of England, Vol. I, p. 614.

<sup>2</sup> S. 82 (c), Negotiable Instruments Act.

<sup>3</sup> Ibid.

<sup>4</sup> *Bank of England v. Vigilante*, (1891) A.C. 107.

<sup>5</sup> Ibid.

drawn. In this respect the bank is "a mere agent or conduit pipe to receive payment of the cheque from the bank on which it is drawn and hold the proceeds at the disposal of the customer".<sup>1</sup> As such agent its duty is to present any cheque, paid in by its customer, for payment with reasonable diligence i.e., within a reasonable time. It has been held that the reasonable time would be presenting the cheque within one day after the receipt thereof where the cheque is drawn on a bank in the same place<sup>2</sup> or forwarding or presenting it on the day following the receipt thereof where the cheque is drawn on a bank in another place.<sup>3</sup> After the expiry of a reasonable time the customer paying in the cheque for collection is entitled to presume that the cheque has been collected and the proceeds thereof have been credited to his account. The customer can, therefore, draw a cheque for an amount not exceeding the amount to be collected after the expiry of such reasonable time. If the bank has failed to collect the cheque in the meantime it cannot dishonour the cheque on the ground of shortage of funds; for there would not have been any shortage had it fulfilled its duty in collecting the cheque promptly. If it dishonours the cheque on this ground the customer can recover damages for wrongful dishonour.<sup>4</sup> If the Bank makes delay in presenting the cheque, the bank will also be liable to the customer for any other loss which the customer may sustain by reason of such delay.<sup>5</sup> Thus the customer pays in a cheque for Rs. 1000/- drawn by X on another bank Y. At the time the cheque is paid in and a reasonable time after that X has sufficient funds in Y. But the Bank does not present the cheque within a fortnight from the date of paying in. Bank Y fails before the cheque is presented. The customer cannot make X liable.<sup>6</sup> Therefore the bank must pay for this loss to the customer. It should be noted, however, that where a collecting bank forwards a cheque drawn on a bank in another place for collection, it may forward it either to its own branch or to an agent in that place. In that case the

<sup>1</sup> Halsbury's Laws of England, Vol. I, p. 590.

<sup>2</sup> Alexander *vs.* Burchfield, (1842) 7 Man. & G. 1061; Rickford *vs.* Ridge, (1810) 2 Camp. 537; Forman *vs.* Bank of England, (1902) 18 T.L.R. 339.

<sup>3</sup> Hart *vs.* Henty, (1861) 10 C.R. (N.S.) 65; Heywood *vs.* Pickering, (1874) 1 E.R. 9 Q.B. 428.

<sup>4</sup> Forman *vs.* Bank of England, *supra*; S. Lubbock *vs.* Tribe, (1838), 3 M. & W. 607, per Lord Abinger, C.B. at p. 612.

<sup>5</sup> S. 34 of the Negotiable Instruments Act [Illustration (a)].

branch or the agent has one day after the receipt of the cheque in which to present the cheque and the reasonable time will not expire after one day after the receipt of the cheque by the collecting bank but after one day after the receipt thereof by such branch or agent.<sup>1</sup> But the collecting bank will be liable in case of delay in presentment by such branch or agent. Presentment need not be actual presentment on the drawee bank but presentment by a recognised clearing house or by post is sufficient.<sup>2</sup> A non-clearing bank may present through a clearing bank.

When a cheque paid to a collecting bank is dishonoured on presentment, the collecting bank must give due notice of dishonour to the customer. The bank usually conveys the notice of dishonour by returning the cheque to the customer which is deemed a sufficient notice of dishonour, if the customer has indorsed it.<sup>3</sup> The bank can also debit the customer with the amount of the cheque if it credited his account with the amount prior to collection.

A customer can draw cheques on the amount of the cheque paid in for collection only after the expiry of a reasonable time necessary for the bank to collect the cheque and complete the necessary book keeping entries.<sup>4</sup> We have already seen what is to be regarded as reasonable time for presentment. But some more time will be necessary between the presentment of the cheque upto the time when the proceeds of the cheque will be available for drawing against for the purpose of collecting the proceeds and crediting them to the customer's account at the collecting bank and to complete the necessary book keeping entries. This time will vary according to circumstances. Thus more time will be necessary for a Calcutta bank to collect the proceeds of a cheque drawn on an Ambala Bank and to make them available for a customer than will be the case when the paying or drawee bank is a Calcutta bank. What will be the reasonable time after which a customer will be entitled to draw against a cheque paid in for collection is to be decided by the facts and circumstances of

<sup>1</sup> *Prideaux vs. Criddle*, (1864) L.R. 4 Q.B. 455.

<sup>2</sup> *Reynolds vs. Chettle*, (1911), 2 Camp. 556.

<sup>3</sup> For rules regarding notice of dishonour see *Sopra. Negotiable Instruments Act.*

<sup>4</sup> *Martelli vs. Williams* (1830), 18 & Ad. 415.

each case. But where a customer is credited with the amount of a cheque paid in for collection prior to the receipt of payment in respect thereof, the customer is at once entitled to draw on it.<sup>1</sup> The bank is, however, entitled to debit the amount if the cheque is subsequently dishonoured on presentation.<sup>2</sup>

#### **Liability of a Collecting Bank to Third Parties :**

A collecting bank incurs liability to a third party who is the true owner of the cheque in case the customer on whose behalf it collects the cheque happens to have no title or a defective title therein. The true owner has only to prove that the customer on whose behalf the collecting bank was acting was not the true owner and had no right to receive payment in respect of the cheque. Such a situation arises where the customer obtained the cheque from the drawer or holder by means of fraud or an offence e.g., theft or where he obtained the same by endorsement or delivery from a person who so obtained it unless he is a holder in due course or the person from whom he obtains it was himself a holder in due course<sup>3</sup>. But even a holder in due course acquires no title where he obtains the cheque by virtue of a forged indorsement by the thief or forger. Thus in all cases except theft or forgery a bona fide holder for value without notice will acquire a valid title as against the true owner. In cases of theft a holder in due course will not acquire a valid title unless the cheque has been perfected so as to be transferable by mere delivery e.g., when a cheque is payable to bearer or indorsed in blank.<sup>4</sup> But in the case of a forged indorsement or a forged cheque, the cheque is never perfected and forgery cannot confer title even to a holder in due course.<sup>5</sup> In collecting uncrossed cheques the bank is liable to the true owner for the value of the cheque if the customer has no title or a defective title thereto. The liability arises in conversion which means a civil wrong or tort consisting of depriving a true owner of his property.<sup>6</sup> But

<sup>1</sup> Capital & Counties Bank *vs.* Gordon (1903) A.C. 240 per Lord Lindley at p. 249.

<sup>2</sup> *Ibid.*, at p. 248.

<sup>3</sup> S. 58 of the Negotiable Instruments Act.

<sup>4</sup> Raphael *vs.* Bank of England (1855) 17 C.R. 161.

<sup>5</sup> For a holder in due course see *Supra* Negotiable Instruments Act.

<sup>6</sup> Capital and Counties Bank *vs.* Gordon (1903) A.C. 210; Fine Art Society *vs.* Union Bank of London (1886) 17 Q.B.D. 705.

in the case of crossed cheques a collecting bank enjoys certain amount of protection. The Negotiable Instruments Act<sup>1</sup> lays down that a banker who in good faith and without negligence receives payment for a customer of a cheque crossed generally or specially to himself shall not, in case the title to the cheque proves defective, incur any liability to the true owner of the cheque by reason only of having received such payment. A banker is to be deemed to receive payment of a crossed cheque even if he credits the customer's account with the amount of the cheque before receiving payment thereof. It is clear that this protection is only limited and a collecting bank will be protected only if it brings itself within the following conditions, namely, (1) that it should act in good faith and without negligence in collecting the cheque, (2) that it should receive payment for a customer is a mere agent and not of its own right, a holder, (3) that the person for whom it acts must be its customer and (4) that the cheque should be crossed generally or specially to the bank. Let us examine these conditions separately.

### (1) Good Faith and Want of Negligence :

The protection granted to a collecting bank is only available when the bank exercises due care and caution in the matter of collection, the want of which necessarily implies negligence and absence of good faith. It is no defence for the bank that the defective title could not have been discovered even with the exercise of due care, for any person who does not exercise reasonable care is outside the protection altogether.<sup>2</sup> Whether a collecting bank has taken reasonable care or has been negligent or not is a question of fact and has to be determined by the facts and circumstances of each case. But the test seems to be "whether the transaction of paying in any given cheque, coupled with the circumstances, antecedent and present, is so out of the ordinary course that it ought to arouse doubts in the banker's mind and cause him to make enquiry".<sup>3</sup> Thus the very nature of the cheque may sometimes cast doubt as to the title of the customer and the

<sup>1</sup> S. 131.

<sup>2</sup> Savory & Co. vs. Lloyds Bank, (1932) 2 K.B., on appeal (1933) A.C. 201.

<sup>3</sup> Commissioners of Taxation vs. English & C.I.L. Bank Ltd., (1920) A.C. 683, 688.

bank must make inquiries and if it receives payment without making such inquiries it will be liable to the true owner. Cases of this kind occur frequently when agents known to be such or appearing to be such from the terms of the cheque pay in the cheque to their own private accounts. Thus where the secretary of a company indorsed a cheque payable to the company and paid it into a private account, it was held that the banker ought to have made inquiries as to his authority to do so before receiving payment on his behalf.<sup>1</sup> This would be so even if a manager of a company is authorised to draw cheques on the company's bankers, where the circumstances may indicate that the manager is exceeding his authority. Thus where the Chief accountant of the plaintiff's branch in Bombay authorised to draw cheques on their bankers, fraudulently drew a number of cheques in favour of his own bankers, namely, the defendants who collected and credited the proceeds to his account, it was held that the defendants were put on inquiry by the fact that large sums of money, which could not be attributed to his salary were being transferred to them by a person who to their knowledge was an agent of the plaintiff and they were liable to the plaintiff for having received payment on the cheque without making the necessary inquiries. A similar view was taken by the House of Lords in *Mallind Bank vs Reckitt*<sup>2</sup> which contains an admirable and exhaustive statement of the law as to the liability of a collecting bank in this respect. There the plaintiff who went abroad employed a solicitor as his agent giving him a power of attorney to sign cheques on his account, without restrictions. The solicitor indorsed some of the cheques payable to the plaintiff in favour of the defendants in order to reduce his overdraft account. It was held that the defendant bank were put on inquiry by the very nature of the cheques which showed that the money was not the money of the customer and that they were negligent in collecting the cheques without proper inquiry. In the same way a collecting bank would be liable if it collects cheques payable to rates collector, secretaries of companies or charitable institutions, and the like, under their official denominations or to a partnership in the firm's name or to

<sup>1</sup> *Hannan's Lake View Central Ltd vs. Armstrong & Co.*, (1900), 16 T.L.R., 236.

<sup>2</sup> *Lloyds Bank vs. Chartered Bank* (1929) 1 K.B. 236.

<sup>3</sup> (1933) A.C. 1.

executors as such and credits them without due inquiries to the private accounts of individuals indorsing them in their representative capacity.<sup>1</sup> Similarly a *per pro* indorsement would put the bank on inquiry and collection of a cheque so indorsed without necessary inquiries would constitute negligence.<sup>2</sup> The necessary inquiries must not only include the authority to indorse but also the authority to pay in and collect the cheque in the manner proposed.<sup>3</sup> A collecting bank may, however, be relieved of liability even in the absence of reasonable care if the true owner is, by his conduct, estopped from denying the validity of the payment or deemed to adopt the payment. Thus in *Morrison v. London County and Westminster Bank*<sup>4</sup> the facts were as follows. The manager of the plaintiff having authority to sign *per pro* drew cheques so signed for a number of years and paid them fraudulently into his private account with the defendant bank who collected the sum. It was held that as regards the earlier cheques the defendants were negligent in so much as they had notice of the agency but nevertheless they were held not liable as on the facts it appeared that the plaintiff adopted the earlier transactions. As regards the later cheques it was held that the defendants were not negligent as the plaintiff by adoption of the earlier transactions led them to believe that the dealings of the manager were authorised and valid. We have already discussed the requisites of acceptance and adoption in connection with payment of cheques.

Apart from the case of negligence in collecting cheques for the purpose of paying in the sum fraudulently so without authority there may be other instances of negligence which would make a collecting bank liable to the true owner. Thus if a bank collects a cheque crossed account payee for a customer who is on the face of the cheque not the payee then he would be liable in the absence of proper enquiries.<sup>5</sup> Omission to detect irregularity in the endorsement would also amount to negligence.<sup>6</sup> Absence of inquiry about a new customer opening an account or to follow up

<sup>1</sup> *Bevan vs The National Bank* (1906) 23 T.L.R. 65

<sup>2</sup> *Bissel vs Fox*, (1885) 53 I.T. 193

<sup>3</sup> *Gompertz vs Cook* (1901) 20 T.L.R. 106

<sup>4</sup> (1914) 3 K.B. 356

<sup>5</sup> *Houle Property Co. vs London County and Westminster Bank* (1915) 84 I.J.K.B. 1846

<sup>6</sup> *Pearson, Tuner and Sons vs London and South Western Bank* (1900) 1 Q.B. 270

a reference given by such customer would also constitute negligence. Thus in *Hampstead Guardians v. Barclays Bank*<sup>1</sup> a person opened an account with the defendant bank with a cheque stolen by him representing that he was the payee thereof. He gave a fictitious address and the bank could by consulting the directory have ascertained that no person of such name was living there. It was held that the bank was neg<sup>l</sup> rent.

### (2) Receipt for Customer:

A collecting bank can claim protection only if it receives payment as the agent of its customer i.e. as a mere conduit pipe for conveying the cheque to the bank on which it is drawn or receiving the money item that bank for their customer. A bank does not cease to be such an agent by the mere crediting crossed cheques in cash before receipt of payment. But when a bank becomes a trustee of the cheque for value in deal with the cheque that but for a forged indorsement it would become the owner thereto, the bank does not collect the chec for the customer but in itself and in such case the bank will be liable to the true owner of the title to the cheque proves to be defective even in the absence of negligence.<sup>2</sup> The bank becomes a trustee of the cheque for value and ceases to be agent for the customer if it pays cash for the cheque across the counter or if the cheque is paid in on the express understanding that it may drawn against it once whether it is lawfully drawn against or not or if the cheque is paid expressly for the reduction of overdraft. But the mere existence of an overdraft, for which the bank would have a lien over the cheque paid in, making the bank a holder for value to the extent of the lien would not take it out of the protection from the bank.<sup>3</sup>

### (3) Customer:

We have seen already that a collecting bank can claim prote

<sup>1</sup> (1923) 39 TLR 229

<sup>2</sup> *Capital and Counties Bank v. Gordon* (1909) AC, 240 per L Macnaghten at pp 245, 246

<sup>3</sup> S 131 of the Negotiable Instruments Act

<sup>4</sup> *Capital and Counties Bank v. Gordon*, *Ibd.*

<sup>5</sup> *Royal Bank of Scotland v. Tottenham* (1894) 2 QB 715, In Re *Farrows Bank*, (1923) 1 Ch 4149

<sup>6</sup> *Clark v. London and County Bank* (1897) 1 QB 552, *Suttess & Briggs* (1922) AC 1, 17.

tion only if it receives payment for a customer. Therefore it becomes very important to appreciate what is actually signified by the word 'customer'. A customer has been defined as a person having habitual dealings with the banker in the nature of ordinary banking business<sup>1</sup>. It necessarily implies a person who has the use and habit of resorting to the bank to do business. Hence an isolated transaction e.g., collecting a cheque for a stranger would not constitute that person a customer.<sup>2</sup> Nor would a person who had been continually cashing crossed cheques across the counter for a number of years be deemed a customer.<sup>3</sup> It was pointed out by Lord Dovye in *Great Western Rail. Co. vs. London and County Banking Co.*<sup>4</sup> that there must be some sort of account, either a deposit or a current account or some similar relation, to make a man a customer of a banker. In a recent case decided by the House of Lords<sup>5</sup> the question which came up for decision was whether a person was a customer in view of the fact that he opened an account only two days prior to the paying in of the disputed cheque. Lord Dunedin in his judgement observed as follows: "the word "customer" signifies a relationship in which duration is not of the essence. A person whose money has been accepted by a bank on the footing that they undertake to honour cheques upto the amount standing to his credit is a customer of the bank irrespective of whether his connection is of short or long standing". But it is submitted that if the account is opened with the disputed cheque the person paying in the cheque will not be regarded as a customer at the time he pays in and the bank will be liable in case the title to the cheque rests with someone else. As Darling J. observed in *Tate vs. Wilts and Dorset Bank*,<sup>6</sup> "He was not a customer at the moment, but he was going to become a customer if the cheque was collected." It seems that the distinction is not between a habitual customer and a new one but between one for whom the bank renders a casual

<sup>1</sup> *Halsbury's Laws of England*, Vol. I, p. 595, 596.

<sup>2</sup> *Mathew vs. Burn & Co.* (1894), 10 T.L.R. 386.

<sup>3</sup> *Great Western Rail Co. vs. London & County Bank Co.* (1901) A.C. 414.

<sup>4</sup> *Ibid.*

<sup>5</sup> *Commissioners of Taxation vs. English, Scottish & Australian Bank* (1920) A.C. 683.

<sup>6</sup> (1899) *Journal of Institute of Bankers*, Vol. XX, p. 376, per Darling J.

service e.g., cashing a cheque for the first time for the purpose of opening an account or for obliging him or someone else and a person who has an account of his own at the bank.

#### (4) Crossing :

A collecting bank can claim protection only if the cheque paid in for collection is crossed generally or specially to itself.<sup>1</sup> If it was not crossed at the time it was paid in the bank, the bank cannot acquire the protection by crossing an uncrossed cheque specially or generally<sup>2</sup>.

#### Bank's Liability as a Holder in Due Course :

We have already seen that except in the case of forged indorsements and theft of a cheque not perfected (i.e., a cheque which has to be indorsed for negotiation) a holder in due course acquires a valid title. Hence where there is no question of forged indorsement, a collecting bank may escape liability if it can establish an independent title to the disputed cheque as a holder in due course excepting where the cheque is crossed "not negotiable". Thus it was held in *Gordon v. London and County Banking Co.*<sup>3</sup> it was held that a cheque crossed "not negotiable" cannot be obtained by a bank as a holder in due course since such a cheque cannot be negotiable and the bank cannot escape liability on that ground. The bank will be regarded as a holder in due course in the following cases (a) where the bank pays cash for the cheque over the counter,<sup>4</sup> (b) where the cheque is paid in expressly in reduction of an overdraft,<sup>5</sup> (c) where the cheque is paid in on express condition of being at once drawn against, and is so drawn against,<sup>6</sup> (d) where the cheque is paid in subject to a lien in favour of the bank,<sup>7</sup> and (e) where an uncrossed cheque is paid in and credited

<sup>1</sup> For general and special crossing see Negotiable Instruments Act ss 124, 125, 126

<sup>2</sup> Capital and Counties Bank *vs* Gordon (1903) A.C. 240

<sup>3</sup> Capital and Counties Bank *vs* Gordon (1903) A.C. 240

<sup>4</sup> (1901) A.C. 414

<sup>5</sup> Halsbury's Laws of England Vol. 1, p. 592.

<sup>6</sup> London and County Bank *vs* Groome (1881), 8 Q.B.D. 288

<sup>7</sup> National Bank *vs* Silke (1891) 1 Q.B. 435, 439.

<sup>8</sup> *Ibid.*, 620.

as cash at once<sup>1</sup>. If a bank becomes a holder in due course of any cheque paid in for collection as in any of the abovementioned cases, it has all the rights of such holder and can sue the parties to it, namely, the drawer and all the subsequent indorsees in its own name in case the cheque is dishonoured on presentation.

### Collection of Bills of Exchange :

A bank is not under any duty to collect bills of exchange for its customers. But if it undertakes to collect a bill for customer, it must present the bill for acceptance and payment in accordance with the provisions of the Negotiable Instruments Act<sup>2</sup> and to give notice of dishonour to the customer in case the bill is dishonoured. This is necessary in order to enable the customer to give notice of dishonour within a reasonable time to the parties he wants to make liable thereon. It has already been noticed that the holder of a bill must give notice of dishonour to the parties he wants to make liable within a reasonable time<sup>3</sup> and in default he may not be able to hold such parties liable. Therefore the bank will be liable to the customer for any loss he may incur as a result of the bank failing to present the bill and to communicate notice of dishonour in due time.

A bank which collects a bill for its customer, to which the customer has no title, is liable to the true owner for conversion. It does not enjoy the protection which is available to it in the collection of crossed cheques<sup>4</sup>. But where the bank becomes a holder in due course of bills given to it for collection it will not be liable to the true owner excepting in the case of forged indorsements. A bank will become a holder in due course of a bill payable to bearer by the mere delivery thereof provided (a) the bank pays cash across the counter or (b) the bill is given expressly in reduction of an overdraft, or (c) the bill is given on the express condition of its being drawn against at once or (d) the bill is paid in subject to the bank's lien or (e) the bill is discounted. In the case of a bill payable to order the bank will be a holder in due course if it is indorsed to the bank and paid in under any one of the conditions mentioned above.

<sup>1</sup> Capital and Counties Bank *vs.* Gordon, *Supra*.

<sup>2</sup> See Negotiable Instruments Act *Supra*.

<sup>3</sup> S. 94 of the Negotiable Instruments Act.

<sup>4</sup> Arnold *vs.* Cheque Bank (1876), 1 C.P.D. 578 at 585.

### Collection of Bankers' Drafts :

Drafts drawn by one office of a bank on another office of the same bank are not cheques since the drawer and the drawee are, in the eye of law, the same person. They cannot, therefore, be crossed and even if they are ostensibly crossed, a bank collecting them for its customer would not enjoy the protection which would be available to it if they were crossed cheques. Hence a collecting bank receiving payment in respect of such drafts for its customer who has no title to them would be liable to the true owner for conversion. But a draft drawn by one bank on another is a cheque and may be crossed and dealt with as such<sup>1</sup>. Therefore a collecting bank receiving payment in respect of a crossed draft drawn by one bank on another would enjoy the same protection as against the true owner as would be available to it in the matter of collecting crossed cheques.

### The Bankers Lien :

A banker may, in the absence of a contract to the contrary, retain, as a security for a general balance of account, any goods deposited with him by a customer if the customer is indebted to the bank on such a general balance of account<sup>2</sup>. This right to retain the property of another for a general balance of account is known as a *general lien* as opposed to a *particular lien* e.g., that of an artificer for his charge on account of labour employed or expenses bestowed upon the identical property retained<sup>3</sup>. This general lien was originally established in England, as regards bankers and others, as a proved usage of trade and at once became a part of the law of merchant as judicially recognised<sup>4</sup>. A banker's lien extends to all bills and cheques paid in for collection and to all securities deposited with the banker by a customer (including share certificates<sup>5</sup>, a pay order<sup>6</sup>, a policy of insurance<sup>7</sup> and a lease<sup>8</sup>) or by a third person on a customer's account and to money paid in by, or to the account of a customer, unless there be a contract,

<sup>1</sup> Halsbury's Laws of England, Vol 1 p 602

<sup>2</sup> S 171 of the Indian Contract Act

<sup>3</sup> Kent, Commn n. 634.

<sup>4</sup> Brandao *vs* Barnett (1846) 12 C.L. & F. 757

Re United Service Co., Johnston's Claim (1871), 6 Ch. App 212.

<sup>5</sup> *Am vs Currie* (1876) AC 564

<sup>6</sup> *Re Bowes* (1886), 33 Ch. D. 586.

<sup>7</sup> *Mutton vs Peat* (1900) 2 Ch. 79.

express or implied, excluding the lien. An agreement excluding the general lien may be expressly provided for or may be implied as when securities are paid in to secure overdrafts upto a specified limit. In such a case the bank cannot claim a lien for any amount exceeding the limit<sup>1</sup>. Similarly he cannot claim a lien on cheques or bills which are paid in specifically for providing funds to meet cheques drawn by the customer or bills accepted by the bank on behalf of the customer, for the bank receives such cheques or bills for a specific purpose which impliedly excludes the general lien.<sup>2</sup> But it seems that the banker's lien will attach to securities paid in for a specific purpose e.g., to secure an overdraft or to meet a particular cheque if they remain with the bank after such overdraft or cheque has been paid off,<sup>3</sup> though doubts have been expressed whether the bank can claim a lien on the securities in such a case.<sup>4</sup>

Where bills or cheques are paid into a bank, a question arises whether the bank receives them as an agent of the customer or as a transferee which makes it a holder in due course. We have already seen under what circumstances the bank will be regarded as a transferee<sup>5</sup>. If the bank receives them as a transferee no question of lien arises, for the bank is entitled to the whole of the proceeds. But if the bank receives them as an agent of the customer, it has a lien on them to the extent of the customer's indebtedness to the bank, if any. But where the bank has a lien it becomes a holder in due course in respect of cheques or bills or a promissory note payable to bearer to the extent of the lien<sup>6</sup> and in such a case the bank can sue for the whole amount of the bill or cheque in case it is dishonoured, holding any surplus over the customer's indebtedness for the customer.

A bank receiving a cheque or bill or note from a customer must present it for acceptance or payment whether it claims a lien in respect thereof or is a transferee for value thereof.

In the absence of an agreement to the contrary whether express

<sup>1</sup> *Re Bowers, Supra.*

<sup>2</sup> *Early v. Turner* (1857), 26 L.J. Ch. 710; *Mercantile Bank of India v. Kochandas Gindumal*, (A.I.R.) 1926 Sind, 223.

<sup>3</sup> *Re London and Globe Finance Corporation* (1902) 2 Ch. 416 per Lord Buckley J.

<sup>4</sup> *Halsbury's Laws of England*, Vol. I p. 621, Note (4).

<sup>5</sup> S. 9 of the Negotiable Instruments Act.

or implied, a banker is entitled to combine all the different accounts kept by the customer in the same right (*i.e.*, not in different capacities as when he has a personal account and another as a trustee), whether deposit or current, or whether at the same branch or different branches, and to exercise his lien on the resulting balance.<sup>1</sup>

In order to be entitled to claim a lien the bank must receive the securities or bills on which the lien is claimed as a banker acting in the course of banking business.<sup>2</sup> Thus the bank cannot claim a lien on securities or valuables deposited with it for safe custody for it receives them not as a banker but as a bailee<sup>3</sup>. Nor can the bank claim a lien on title deeds casually left at the bank after a refusal by it to advance money on them.<sup>4</sup>

The banker's lien is not like the ordinary lien which is only a passive right.<sup>5</sup> It gives the banker the right of a pledgee so as to enable him to sell the negotiable instruments or securities on which he has the lien in case the customer fails to repay his debts within the time fixed or where no time is fixed after a reasonable notice to the customer to pay and the failure of the customer to pay within the time fixed by the notice.<sup>6</sup>

#### **Letters of Credit and Documentary Bills :**

A letter of credit is a document addressed to a specified person or generally by a bank requesting the addressee, where he is specified or any person to whom it may be presented, where the addressee is not specified, requesting him to make payments or advances or extend credit (such as allowing the facility to draw cheques) to the person to whom the letter is granted upto a specified amount or intimating him that the grantee of the letter is authorised to draw bills of exchange on the bank upto a specified amount. Where the addressee is specified the letter is 'special' and where the letter is addressed to anyone to whom it may be

<sup>1</sup> *Garnet vs. M'Kewan* (1872) L.R. 8 Ex. 10 ; *Prince vs. Oriental Bank Corp.* (1878) 3 A.C. 325, 333.

<sup>2</sup> *Brandao vs. Barnett* (1846) 12 C. & F. 787.

<sup>3</sup> *Cuthbert vs. Roberts, Lubbock & Co.*, (1909) 2 Ch. 226, C.A.

<sup>4</sup> *Legas vs. Derrion*, (1817) 7 Taunt. 278.

<sup>5</sup> See lien under the Chapter on Mortgage.

<sup>6</sup> *Burdick vs. Sewell* (1884), 13 Q.B.D. 159 ; *Ex parte Official Receiver, Re : Moritt* (1886) 18 Q.B.D. 222, at p. 232.

presented, it is called "general" or "open". The letter is generally addressed to an agent of the bank or to a bank at another place. Letter of credit play a very important role in financing international trade and commerce and obviates the necessity for a customer, carrying on trade between different countries or places, to keep his funds tied up in different places.

Where the letter is a request to pay money or extend credit to the grantee, the bank becomes liable to the party so paying or extending credit on the production of the letter.<sup>1</sup> If the letter is special only the addressee can act on the letter and no one except the addressee can make the bank liable by acting on it. But if the letter is general any one acting on it may make the bank liable.

Where the letter simply contains an authority to the grantee to draw bills of exchange on the bank upto a specified amount, it is meant to be shown to third parties conveying the intimation to them that there is a binding contract whereby the bank will accept bills of exchange drawn on it by the grantee upto the specified amount. If any person acts on the letter e.g., by discounting a bill drawn by the grantee and paying for it, he can force the bank to accept the bill and pay for it.<sup>2</sup> Where a bank grants a letter of this kind to a customer, the letter usually provides that the customer can draw bills only against actual shipments of goods, bills of lading or other documents of title and that the acceptance of bills drawn by the customer is conditional upon the forwarding of such documents of title to the bank. Any person presenting a bill, drawn by the customer on the authority of such a letter, to the bank for acceptance must, therefore, see that the documents of title reach the bank before or at the time it is called upon to accept ; for otherwise the bank will not be liable to accept the bills so presented without the documents.<sup>3</sup> A letter of credit with a condition about documents is called a "documentary letter of credit". If such a letter of credit describes the goods against which the bills are to be drawn, it has been held that the bank

<sup>1</sup> Morgan *vs.* Lariviere (1875), L.R. 7 H.L. 423.

<sup>2</sup> Maitland *vs.* Chartered Mercantile Bank of India, London and China (1869) 38 L.J. Ch. 363 ; Union Bank of Canada *vs.* Cole (1877), 47 L.J. C. 100 at 109 ; Re Agra and Masterman's Bank, Ex parte Asiatic Bar Corporation (1867), 2 Ch. App. 391.

<sup>3</sup> Ex parte Brett, Re Howe (1891) 6 Ch. App. 838, 841.

is not bound to accept the bills if the goods shipped do not correspond exactly with the description given in the letter whether they are considered to be the same in the market or not.<sup>1</sup>

A person who acts on a documentary letter of credit e.g., one who discounts a bill drawn by the customer and receives the documents or an indorsee from him, does not acquire any right or title to the goods to which the documents relate. His right is against the bank and the drawer personally.<sup>2</sup> But the bank acquires a lien and the right of a pledgee over the goods on its acceptance of the bill and the receipt of the documents.<sup>3</sup> So if the customer fails to pay for the bill at maturity after the bank's acceptance and the bank has to pay the acceptance, the bank may realise the amount of the bill paid by it by selling the goods. But it seems that before selling the goods the bank should give notice to the customer to pay the money within a reasonable time and if the customer makes default the bank may sell the goods and realise the amount paid.<sup>4</sup>

Letters of credit are not negotiable. Therefore a person who pays money or extends credit to any one other than the grantee of the letter cannot recover the money so paid from the bank which issued the letter. If the grantee has paid or deposited money with the bank which issued the letter for obtaining it, he may recover any money paid wrongly or mistakenly by the issuing bank to any other person who might have obtained or used the letter by fraud or any other offence.<sup>5</sup>

Letters of credit which are issued to travellers in foreign countries are usually of the following varieties, namely, (1) circular letters of credit, (2) circular notes and (3) traveller's cheques.

(1) A circular letter of credit is usually in the form of a request by a bank to its agents and correspondents in foreign countries to honour the cheques and drafts of the grantee upto a specified amount which the issuing bank undertakes to honour on presentation. These letters are obtained either by paying or depositing cash to the issuing bank or giving a guarantee for the

<sup>1</sup> Rayner & Co. Ltd. vs. Hambros Bank (1942) 2 A.E.R. 694.

<sup>2</sup> Re Barned's Banking Co. (1871), L.R. 5 H.L. 157 at 167.

<sup>3</sup> Re Barned's Banking Co., *Supra*. Ex parte Brett, Re Howe (1871) 6 App. 838 at 841.

<sup>4</sup> Halsbury's Laws of England, Vol. 1 p. 624, 625.

<sup>5</sup> Re : M'Dr. vs. Union Bank of Scotland (1854), 1 Macq. 513.

payment of the amount of cheques or drafts which the issuing bank undertakes to honour. A circular letter of credit is known as a guarantee letter of credit where it is obtained by the grantee by furnishing guarantee for the amount. (2) A circular note is akin to a circular letter of credit excepting that it is generally for a certain round sum in the currency of the country of the issuing bank and is accompanied by a letter of indication. (3) Traveller's cheques are akin to circular notes and are current for a fixed period and are almost always signed by the holder at the time of the issue and signed again in the presence of the person who is requested to pay at the time of payment.

### **Safe Custody of Valuables:**

The position of a bank in accepting deposits of property or valuables for safe custody is like that of a bailee.<sup>1</sup> As such he is bound to take as much care of the goods deposited with him as a man of ordinary prudence would under similar circumstances, take of his own goods of the same description. In the absence of any special contract his liability is not like that of an insurer as to make him liable to the owner for any loss or damage to the goods. If he takes the amount of care mentioned above he will not be liable for the loss, destruction or deterioration of the goods unless he agrees to accept for value any higher liability at the time of deposit. An acknowledgement by the banker that he receives the goods for safe custody does not make his liability any the higher. He is not also liable for the criminal acts of his employees which there was no ground for anticipating.<sup>2</sup> But if he knowingly employs a dishonest person he would be answerable for the latter's acts as in employing the latter he cannot be regarded as exercising the amount of care which is required of him. He would also be liable to the owner if he delivers the goods to a wrong person. This would be so even if he is not negligent and the goods are obtained from him by means of an order to which the owner's signature has been forged.<sup>3</sup> That is why a

<sup>1</sup> Giblin *vs* McMullen (1868) L.R. 2 P.C. 317 Re United Services Johnston's Claim (1871) 6 Ch. App. 212

<sup>2</sup> S. 151 of the Contract Act

<sup>3</sup> Ross *vs* Hill (1846) 2 C.B. 877

<sup>4</sup> Cheshire *vs* Bailey, (1905) 1 K.B. 237

<sup>5</sup> Stephenson *vs* Hart (1828) 3 Bing. 476, McKean *vs* McMillan L.R. 6 Ex. 36

bank is entitled to refuse delivery of goods and retain them until it is satisfied about the identity of the person or the genuineness of the order requiring delivery where the bank is suspicious about such identity or genuineness.

#### Discounting Bills :

Apart from collecting and paying bills on behalf of customers, one of the most important functions of a modern bank is the discounting of bills brought to it by a customer or any one else. In performing this function a bank renders a most valuable service to the commercial world at large. The importance of this service may be illustrated by the following example. A exports 100 bales of Tibetan wool of the value of Rs. 1,00,000/- from Calcutta to B in London. Between the date on which he consigns the wool and the date on which the same reaches B and payment is realised thereon a long time may elapse during which A's money will be locked up without any chance of being invested in further business. A might have to sit idle during this time unless he has sufficient funds at his disposal. But this difficulty is obviated by the system of discounting bills by banks which is usually done in the following manner. A draws a bill of exchange on B for Rs.10,000/- payable at sight or after sight, as soon as the goods are shipped. He then goes to his bank with the bill and bills of lading and other documents evidencing the consignment of the goods. The bank, if satisfied with the genuineness of the bill, discounts the bill by paying A the amount of the bill less a certain sum which is known as the discount charge or the rate of discount and after retaining the bill of lading and the other documents. The bank then sends the bill either to its branch or an agent in London along with the bill of lading and the other documents for presenting it to B for acceptance or payment where no acceptance is necessary. On presentation of the bill to B, B takes the bill of lading and the other documents which alone would give him the right to take delivery of the goods after accepting the bill or paying for the same as the case may be.

A bank is said to discount a bill when it takes a bill at once as a transferee for value. Where the bill is negotiable by mere delivery e.g., when it is payable to bearer<sup>1</sup> the bank becomes a

<sup>1</sup> See 47 of the Negotiable Instruments Act.

holder in due course by discounting the bill, even without the indorsement of the customer, if it takes the bill without notice of any defect in the customer's title,<sup>1</sup> if any, and it can sue the drawee or acceptor or the drawer of its own right. But if the bill is payable to order it can be negotiated only by indorsement and delivery and without the indorsement of the customer the bank will be merely a transferee for value and not a holder in due course. The difference between a transferee for value and holder in due course is that a transferee cannot sue on the bill in his own name, nor can he negotiate it to a third party until the transferor indorses the instrument.<sup>2</sup> The right of the transferee is like that of an assignee of the ordinary chose-in-action and if he has paid value for the transfer he acquires the right to compel the transferor from whom he has taken the instrument to put his indorsement<sup>3</sup> which may be enforced by a suit if the transferor refuses to do so.<sup>4</sup>

When a bank receives a bill from a customer it is question of fact in every case as to whether the bill is taken for collection or as security for a loan or overdraft or for discount. Where the bank receives the bill for collection the bank does not become a holder in due course or transferee for value and it remains liable to the true owner of the bill in case the customer's title to the bill proves defective.<sup>5</sup> But even in the case of a bill paid in for collection the bank will not be liable to the true owner if it becomes a holder in due course in respect of the bill unless the bill has been negotiated by a forged indorsement.<sup>6</sup> Where, however, a bank receives a bill from a person who is not a customer the presumption is that the bill has been discounted. A bank becomes a holder in due course of a bill discounted by it by mere delivery thereof, if it is payable to bearer, and by delivery and indorsement, if it is payable to order provided it has no notice of any defect in the title of the person paying in the cheque.<sup>7</sup> If the bank is the holder of a bill in due course

<sup>1</sup> S. 9 of the Negotiable Instruments Act.

<sup>2</sup> *Harrop vs. Fisher*, (1861) 10 C.R. (N.S.) 196.

<sup>3</sup> *Walker vs. Neary* (1904) 21 T.L.R. 146; Specific Relief Act, S.R. Illus.

<sup>4</sup> *Rose vs. Sims* (1830) 18 & Al. 521.

<sup>5</sup> See *Supra*.

<sup>6</sup> Capital and Counties Bank *vs. Gordon* (1903) A.C. 240; See *Supra* for conditions under which a bank will become a holder in due course.

<sup>7</sup> S. 9 of the Negotiable Instruments Act.

it will not be liable to the true owner if the transferor's title proves defective except in the case of forged indorsement by the transferor or someone from whom the customer took the bill. But the bank will be liable to the true owner if it discounted a bill payable to order without a proper indorsement, for in such a case the bank will be a mere endorser for value or assignee and not a holder in due course and in consequence the assignment subject to all defects in the title of the assignor.

In the case of dishonour of a bill discounted by bank for its customer, they can debit the customer's account with the amount of the bill where the customer's indorsement is on the bill. Where the customer's indorsement is not on the bill the bank cannot debit the customer's account and has to pay with the probability referred to in the rule <sup>1</sup> ' *rin te ec le v hic'*

A bank cannot also debit in money due to customer as a cover in, in the name of the customer, of the bill discounted for the customer being, or rendered, dishonoured. It seems however that the bank can do so in the event of the customer's insolvency before the maturity of the bill. The rule appears to be that in the event of the customer's insolvency all the properties and assets of the customer will go to the Official Assignee or receiver as he may be including the moneys in the hands of the bank subject to the lien of the latter, if any, existing at the moment. But the bill being in the hands of the bank for any prospective dues which the bank may have in case the bill is dishonoured at maturity. If the money is handed over to the Official Assignee or Receiver and then the bill is dishonoured the bank will have no claim to claim a lien on such the dishonour of the bill. Therefore it seems reasonable that in such a case the bank may return a sufficient sum to cover against any prospective loss which may be caused by the dishonour of the bill.

### **Loans and Advances by Bankers :**

One of the principal functions of a bank is to give loans and advances to customers and others out of the funds at its dis-

<sup>1</sup> Halsbury's Laws of England, Vol 1 p 629

<sup>2</sup> Boweng's Foreign and Colonial Gas Co., (1874), 22 W.R. 740

<sup>3</sup> Halsbury's Laws of England, Vol 1, 629, 630

posal for the purpose of making profits. The loans may be given with or without security. Where loans are given on the security of mortgages in immoveable property the ordinary law of mortgage will prevail. Where loans are given on securities or negotiable instruments or other kinds of moveable property the position of the bank is like that of a pledgee.<sup>1</sup> It has the right to sell the goods pledged with it if the borrower fails to pay within the time fixed or, where no time is fixed, after the expiry of the time within which he is required to repay by a notice given by the bank fixing a reasonable time within which he is required to pay.<sup>2</sup>

Where a loan given by a bank is secured by documents of title e.g., a railway receipt or a bill of lading, the bank acquires the rights of a pledgee in respect of the goods, to which the documents refer and does not lose such rights by parting with the custody of the documents or by entrusting them to the borrower or his agent for the special purpose of dealing conveniently with the goods e.g. for collecting them from the Port Trust and putting them into the bank's godown.<sup>3</sup> If the borrower commits a fraud by obtaining further advances from other persons on the security of the same documents while they are given to him by the bank for such special purpose, the bank's title to the goods will not be affected by the interests of these other persons so defrauded even though such fraud would not have been committed but for the bank parting with the custody of the documents.<sup>4</sup> But the bank will not be protected where it parts with the custody of the documents or carelessly leaves them with the borrower for no such special purpose and an innocent third party is defrauded thereby.

If the borrower has no title or a defective title to any security or document of title, or moveable property on the security of which a bank advances a loan, the true owner can recover such security or document or moveable property from the bank or hold it liable for damages for conversion in case it has disposed of or dealt with the same except in the following cases :—

<sup>1</sup> *Burdick vs. Sewell* (1884), 13 Q.B.D. 159 ; *Ex parte Official Receiver, Re Moritt* (1886) 18 Q.B.D. 222.

<sup>2</sup> See the Contract Act, *Supra*, for the rights of a pledgee.

<sup>3</sup> *Mercantile Bank of India vs. Central Bank of India* (1937) 65 I.A. 75.

<sup>4</sup> *Ibid.*

- (a) Where the borrower as a mercantile agent of the owner has obtained possession of the security, goods or document with the consent of the true owner and pledges the same to the bank which accepts them in good faith and without notice of the want of authority of the borrower.<sup>1</sup>
- (b) Where the borrower having sold the goods or security continues to be in possession of the goods or security or the documents relating to the goods and pledges the same himself or through a mercantile agent to the bank which receives the same in good faith and without notice of the previous sale.<sup>2</sup>
- (c) Where the borrower, having bought or agreed to buy the goods or security, obtains possession of the goods or documents relating thereto or the security before paying the price thereof and pledges the same himself or through his mercantile agent to the bank which receives them in good faith and without notice of the seller's lien for the unpaid price.<sup>3</sup>
- (d) Where the borrower obtains possession of the goods or security under a voidable contract e.g. one tainted by fraud or duress and pledges the same before the contract has been rescinded by the true owner and the bank receives the same in good faith and without notice of the defect in the borrower's title.<sup>4</sup>
- (e) Where the true owner is estopped by his conduct from disputing the title of the bank.<sup>5</sup>

Where the bank accepts a negotiable instrument payable to bearer as security for a loan, the bank becomes a holder in due course to the extent of its lien and can realise its dues by sale or negotiation of the instrument and retain the same as against the true owner whether the borrower had any title in the instrument or not.<sup>6</sup> Where, however, the bank accepts a negotiable instru-

<sup>1</sup> S. 178 of the Contract Act ; S. 27 of the Sale of Goods Act

<sup>2</sup> S. 30(1) of the Sale of Goods Act.

<sup>3</sup> S. 30(2) of the Sale of Goods Act .

<sup>4</sup> S. 178 of the Contract Act.

<sup>5</sup> S. 27 of the Sale of Goods Act ; See also the discussion under the heading *estoppel*—in the Chapter on sale of goods *Supra*.

<sup>6</sup> S. 9 of the Negotiable Instruments Act ; See *Supra* under the heading “Bank's liability as a holder in due course.”

ment, payable to order as security for a loan the bank will become a holder in due course, if the bill is indorsed in its favour, to the extent of its lien unless the indorsement of the borrower or some other previous indorsement is forged. Where the indorsement is forged the bank will be liable to the true owner unless the bill came into the possession of the borrower under any one of the circumstances mentioned above so as to estop the true owner from disputing the title of the bank.

#### Pass Book :

We have already seen that a bank provides its customer with a pass book at the time of the opening of an account by the customer. The bank periodically records all the payments in as well as all the drawings out by the customer. Entries in the pass book to the credit of the customer<sup>1</sup> are *prima facie* evidence against the bank and the customer is entitled to act on them e.g. by issuing cheques for the amount shown to be lying to his credit.<sup>2</sup> Similarly entries to the debit of the customer are *prima facie* evidence against the customer when he returns the pass book without objection. But the entries in the pass book are not in all cases conclusive and binding on the bank or the customer.<sup>3</sup> Thus credits mistakenly entered<sup>4</sup> or fraudulently entered<sup>5</sup> by a bank official cannot be relied on by the customer and rectified by the bank within a reasonable time unless the customer has acted on such entries and altered his position e.g. by issuing a cheque in favour of a third party and incurring liability thereunder.<sup>6</sup> Similarly if a customer fails to notice or object to a debit entry in respect of a cheque to which his signature was forged and which was paid by the bank before he returns the pass book, he cannot be precluded from recovering the amount paid on such cheque when he comes to know of it<sup>7</sup> as there is no duty cast on the customer to examine the pass

<sup>1</sup> Akro Kerr (Atlantic) Mines Ltd. *vs.* Economic Bank (1904) 2 K.B. 465.

<sup>2</sup> Shunker Das *vs.* Punjab National Bank, 62 I.C. 472.

<sup>3</sup> Commercial Bank of Scotland *vs.* Rhind (1860) 3 Macq. 643.

<sup>4</sup> Br. & N. E. Bank *vs.* Zolztein, (1927) 2 K.B. 92.

<sup>5</sup> Mowji Shamji *vs.* National Bank of India, 25 Bom. 499, 515 ; Skerring *vs.* Greenwood (1825) 4 H & C 281, 289 ; Capital & Counties Bank *vs.* Gordon (1903) A.C. 240, 249.

<sup>6</sup> Walker *vs.* Manchester & Liverpool District Banking Co., (1913) 108 : L.T. 728.

book from time to time.<sup>1</sup> In the same way a bank cannot retain moneys paid in by a customer on the ground of its omission to enter it in the pass book and the failure of the customer to notice the omission or object to the same.<sup>2</sup>

It has in some cases been held that where a periodical balance has been struck in the pass-book and the customer returns the pass book without objection, the balance so struck becomes evidence of a stated and settled account between the bank and the customer.<sup>3</sup> But the better opinion seems to be that in the absence of independent evidence of an implied or express agreement whereby the bank and the customer accept the balance so struck as constituting a stated and settled account the mere fact that such balance has been struck in the pass book without any objection being raised by the customer would not be a conclusive evidence of a stated or settled document.<sup>4</sup>

### **Special Provisions for Banking Companies :**

We have already seen that the Indian Companies Act, 1913 as amended by the companies amendment Act, 1936 makes certain special provisions for banking companies for the purpose of preventing the growth and continuance of mushroom banks. We may note these provisions as follows :

### **Restriction in the number of Partners in a Banking Business:**

No company, association or partnership consisting of more than ten persons can carry on the business of banking unless it is registered as a company under the Indian Companies Act.<sup>5</sup> Any company, association or partnership carrying on the business of banking in contravention of this provision is an illegal association<sup>6</sup> and cannot sue third parties on contracts made by it.<sup>7</sup>

<sup>1</sup> Kepitagalla Rubber Estates Ltd. vs. National Bank of India Ltd., (1909) 2 K.B. 1010.

<sup>2</sup> Halsbury's Laws of England, Vol. 1, p. 619.

<sup>3</sup> Blackburn Building Society vs. Cunliffe Brookes & Co., (1882) 22 Ch. D. 61 at 71, 72.

<sup>4</sup> Vagilano vs. Bank of England (1889) 23 Q.B.D. 243 at 263 (Court of Appeal).

<sup>5</sup> S. 4(1) of the Indian Companies Act, 1913.

<sup>6</sup> Padstow Total Loss Association (1882) 20 Ch.D. 137; Naidu vs. Mudaliar (1918) 50 I.C. 513.

<sup>7</sup> Jennings vs. Hammond (1882) 9 Q.B.D. 225; Senaji vs. Pannaji (1930) P.C. 300.

Every member of any such illegal association is personally liable for all liabilities incurred in such business<sup>1</sup> and punishable with fine not exceeding Rs. 1000/-.<sup>2</sup> In the case of joint families or partnerships consisting of two or more joint families carrying on the business of banking, the minor members are to be excluded in computing the maximum number of members allowed to carry on the business of banking without being formed into a company.<sup>3</sup> The purpose of this provision is to bring big banking concerns under the checks and control of the Indian Companies Act so that the interest of customers dealing with these concerns may be protected.

#### **Limitation of Activities of Banking Companies :**

No company formed after the commencement of the Indian Companies (Amendment) Act, 1936, for the purpose of carrying on business as a banking company or which uses as part of its business name the word "bank," "banker" or "banking" can be registered as a company unless the memorandum limits the object of the company to the carrying on of the business of accepting deposits of money on current account or otherwise subject to withdrawal by cheque, draft or otherwise along with some or all of the forms of businesses specified in S. 277 F<sup>1</sup> and no banking company whether incorporated in or outside British India, can, after the expiry of two years from the commencement of the Indian Companies (Amendment) Act, 1936, carry on any form of banking business other than those specified in S. 277 F.<sup>2</sup>

#### **Restriction on the Employment of Managing Agent :**

No banking company can, after the expiry of two years from 1st July, 1944 employ or be managed by a managing agent, or any person whose remuneration or part of whose remuneration takes the form of commission or a share in the profits of the Company, or any person having a contract with the Company

<sup>1</sup> S. 4(4), *Ibid.*

<sup>2</sup> S. 4(5), *Ibid.*

<sup>3</sup> S. 4(3), *Ibid.*

<sup>4</sup> S. 277 G (i).

<sup>5</sup> S. 277 G (2).

for its management for a period exceeding five years from 1st July, 1944.<sup>1</sup>

### **Capital Requirements and Restriction on Commencement of Business.**

No banking company incorporated on or after the 1st day of January, 1937 can commence business, unless shares have been allotted to an amount sufficient to yield a sum of at least Rs. 50,000/- as working capital and unless a declaration duly verified by an affidavit signed by the directors and the manager that such a sum has been received by way of paid-up capital has been filed with the Registrar. No banking company whether incorporated in or outside British India, if incorporated on or after 15th January, 1937, shall after the expiry of two years from 1st July, 1944, carry on business in British India unless it satisfies the following conditions, namely –

- (a) that the subscribed capital of the Company is not less than half the authorised capital and the paid-up capital is not less than half the subscribed capital, and
- (b) that the capital of the company consists of ordinary shares only or ordinary shares and such preference shares as may have been issued before the 1st of July 1944
- (c) that the voting rights of all shareholders are strictly proportionate to the contribution made by the share holders to the paid up capital of the Company.<sup>2</sup>

### **Prohibition of Charge on unpaid Capital :**

No banking company can create any charge upon any unpaid capital of the company and any such charge shall be invalid.<sup>3</sup> This provision does not seem to affect any such charge created before the commencement of the Companies Amendment Act, 1936, for this provision was not existent before. The general rule of construction is that the repeal or amendment of an Act does not affect a right already in existence unless a contrary intention is made out expressly or by implication.<sup>4</sup> "The appli-

<sup>1</sup> S. 277 H.H. (This section has been inserted by the Companies Amendment Act IV of 1944 which came into force on 1st July, 1944)

<sup>2</sup> S. 277 I as amended by the Amendment Act of 1944.

<sup>3</sup> S. 277 J.

<sup>4</sup> Chowdhury Guraran v. Akhour, I.L.R. 6 Pat. 296.

cation of an Act is when the parties begin to move under it.<sup>1</sup> This provision is designed to protect the interests of the creditors of the company by keeping the unpaid capital available for them in case the company becomes insolvent.

#### **Revenue Fund :**

Every banking company must, after the commencement of the Indian Companies (Amendment) Act, 1936, and in the case of a banking company incorporated before that Act, after the expiry of two years from such commencement, maintain a reserve fund<sup>2</sup> and transfer, out of the declared profits of each year and before any dividend is declared, a sum equivalent to not less than twenty per cent of such profits to the reserve fund until the amount of the said fund is equal to the paid up capital.<sup>3</sup> A banking company must invest the amount standing to the credit of its reserve fund in Government Securities or in securities mentioned or referred to in S 20 of the Indian Trusts Act, 1882 or keep deposited in a special account to be opened by the company for the purpose in a scheduled bank as defined in clause (e) of S. (2) of the Reserve Bank of India Act, 1934.<sup>4</sup>

#### **Cash Reserve :**

Every Banking company excepting a scheduled bank must maintain by way of cash reserve in cash a sum equivalent to at least one and a half per cent of the time liabilities and five per cent of the demand liabilities of such company and file with the Registrar before the tenth day of every month (three copies of) a statement of the amount so held on the Friday of each week of the preceding month with the particulars of the time and demand liabilities of each such day.<sup>5</sup> "Demand liabilities" means liabilities which must be met on demand, such as the amount standing in the current account of a customer which may be drawn against at any time, and "time liabilities" means liabilities which need not be met on demand, e.g. fixed deposits of customers.

<sup>1</sup> Keshoram vs. Nandolal, 54 I.A. 152.

<sup>2</sup> S. 277 K(1).

<sup>3</sup> S. 277 K(2).

<sup>4</sup> S. 277 K(3).

<sup>5</sup> S. 277 L(1).

<sup>6</sup> S. 277 L(2).

### **Penalties :**

If default is made in complying with the above provisions relating to limitation of activities of banking company, or the employment of managing agent, or the prohibition of charge on unpaid capital or requirements of Reserve Fund, every director or other officer of the company who is knowingly and wilfully a party to the default is liable to a fine not exceeding Rs. 500/- for every day during which the default continues. If default be made in filing the statement relating to cash reserve, every such director or officer will be liable to a fine not exceeding Rs. 100/- for every day during which the default continues.<sup>1</sup>

### **Restriction on Nature of Subsidiary Companies and the Holding of Shares:**

A banking company except one incorporated before the commencement of the companies Amendment Act, 1936, cannot form a subsidiary company except one formed for the purpose of undertaking and executing trusts or undertaking the administration of estates as executor, trustee or otherwise and for such other purposes set forth in S. 277F as are incidental to the business of accepting deposits of money on current account or otherwise.<sup>2</sup> A banking company, formed after the commencement of the Amendment Act of 1936, cannot also hold shares in any other company, excepting in such subsidiary company as is allowed to be formed by the company, of an amount exceeding forty per cent of the issued share as a pledgee, mortgagee or absolute owner thereof.<sup>3</sup> Noncompliance with this provision is visited with the same penalty as mentioned above.

### **Power of Court to Stay Proceedings or Grant a Moratorium:**

The court may, on the application of a banking company which is temporarily unable to meet its obligations, make an order staying the commencement or continuance of all actions and proceedings against the company for a fixed period of time on such terms and conditions as it may think fit and proper and may from time to time extend the period.<sup>4</sup> The application of

<sup>1</sup> S. 277 L(4).

<sup>2</sup> S. 277 M(1).

<sup>3</sup> S. 277 M(2).

<sup>4</sup> S. 277 N(1).

the company must be accompanied by a report of the Registrar provided that in the case of extreme urgency the court may grant interim relief pending the hearing of the application without the Registrar's report.<sup>1</sup> But the Registrar's report must be forthcoming before the final order is made. The Registrar is entitled at the cost of the company to investigate the financial condition of the company and for such purpose to have the books and documents of the company examined by an accountant holding a certificate issued by the Governor General in Council entitling him to be an auditor of companies.<sup>2</sup> This provision is intended to allow an otherwise solvent company a breathing time so as to enable it to overcome a temporary shock e.g. war or civil commotion and realise its assets and readjust its affairs. But this provision cannot be used to keep an insolvent company continuing its operations under the protection of the court and to prevent those who had dealings with the company from seeking legal remedies to which they would otherwise have been entitled.<sup>3</sup>

#### **Balance Sheet :**

The balance sheet and profit and loss account or income and expenditure account of every banking company must be signed by the manager or managing agent (if any) and, where there are more than three directors of the company, by at least three of those directors and, where there are not more than three directors, by all the directors.<sup>4</sup> As regards laying the balance sheet and profit and loss account or income and expenditure account before the shareholders and filing the same with the Registrar, a banking company is subject to the same rules as an ordinary company.<sup>5</sup>

#### **Submission of Statements :**

Every banking company must, before it commences business and also on the first Monday in February and the first Monday in August in every year during which it carries on business must make a statement in the following form which is included in

<sup>1</sup> S. 277 N(2).

<sup>2</sup> S. 277 N(1).

<sup>3</sup> Benares Bank Ltd. (1939) AIL 726.

<sup>4</sup> S. 133 (1).

<sup>5</sup> S. 136 (1).

the third schedule of the Indian Companies Act, 1913 as Form No. G, or as near thereto as possible.<sup>1</sup>

**Form G.**  
**(Schedule III)**

The share capital of the company is Rs. divided into shares of Rs. each.

The number of shares issued is Calls to the amount of Rs. per share have been made, under which the sum of Rs. has been received.

The liabilities of the company on the thirty-first day of December (or thirtieth of June) were—

Debts owing to Sundry persons by the company :  
Under decree, Rs.  
On mortgages or bonds, Rs.  
On notes, bills or hundis Rs.  
On other contracts, Rs.  
On estimated liabilities, Rs

The assets of the company on that day were—

Government securities (stating them), Rs  
Bills of Exchange, hundies and promissory notes Rs.  
Cash at the bankers, Rs.  
Other securities Rs.

**Publication of the Statement and the Balance Sheet :**

A copy of the statement together with a copy of the last audited balance sheet laid before the members of the company must be kept displayed until the display of the next following statement in a conspicuous place in the registered office of the company, and in every branch office or place where the business of the company is carried on.<sup>1</sup> Every member and every auditor of the company is entitled to a copy of the statement on payment of a sum not exceeding eight annas.<sup>2</sup> If a company makes default in complying with the requirements of this section, it will be liable to a fine not exceeding Rs. 50/- for every day during

<sup>1</sup> S. 136 (2).  
<sup>2</sup> S. 136 (3).

which the default continues and every officer of the company who knowingly and wilfully authorises or permits the default will be liable to the same penalty<sup>1</sup>

### **Investigation of Affairs :**

The Central Government may appoint one or more competent inspectors to investigate the affairs of a banking company, having a share capital on the application of members holding not less than one fifth of the shares issued.<sup>2</sup> The application must be supported by such evidence as the Central Government may require for the purpose of showing that the applicants have good reason for, and are not actuated by malicious motives in, requiring the investigation, and the Central Government may, before appointing an inspector, require the applicants to give security for payment of the costs of the inquiry. All persons who are or have been officers of the company must produce to the inspectors all books and documents in their custody or favour relating to the company and must answer on oath all questions asked by the inspectors relating to the business of the company, failing which they will be liable to a fine not exceeding Rs. 50/- for each offence<sup>3</sup>. The report of the inspector must be forwarded to the Central Government and will serve as evidence in any legal proceeding<sup>4</sup>.

<sup>1</sup> S. 136 (4).

<sup>2</sup> S. 138 (1)

<sup>3</sup> S. 139.

<sup>4</sup> S. 140(1), (2) & (3)

<sup>5</sup> S. 141(1) & S. 143.



# **Hand Book of Commercial Law**

**PART II**



# The Indian Contract Act, 1872.

[As modified up to the 15th November, 1943.]

Preamble Whereas it is expedient to define and amend certain parts of the law relating to contracts; It is hereby enacted as follows :—

## Preliminary.

Short title 1 This Act may be called the Indian Contract Act, 1872.

Extent, Commencement It extends to the whole of British India; and it shall come into force on the first day of September, 1872.

\* \* \* nothing herein contained shall affect the provisions of any Statute, Act or Regulation repealed not hereby expressly repealed, nor any usage or custom of trade, nor any incident of any contract, not inconsistent with the provisions of this Act.

2 In this Act the following words and expressions are used in the following sense, unless a contrary intention appears from the context.

(a) When one person signifies to another his willingness to do or to abstain from doing anything, with a view to obtaining the assent of that other to such act or abstinence, he is said to make a proposal.

(b) When the person to whom the proposal is made signifies his assent thereto, the proposal is said to be accepted. A proposal, when accepted, becomes a promise.

(c) The person making the proposal is called the "promisor", and the person accepting the proposal is called the "promisee".

- (d) When, at the desire of the promisor, the promisee or any other person has done or abstained from doing, or done or abstained from doing, or promises to do or to abstain from doing, something, such act or abstinence or promise is called a consideration for the promise.
- (e) Every promise and every set of promises, forming the consideration for each other, is an agreement.
- (f) Promises which form the consideration or part of the consideration for each other are called reciprocal promises.
- (g) An agreement not enforceable by law is said to be void.
- (h) An agreement enforceable by law is a contract.
- (i) An agreement which is enforceable by law at the option of one or more of the parties thereto, but not at the option of the other or others, is a voidable contract.
- (j) A contract which ceases to be enforceable by law becomes void when it ceases to be enforceable by law.

## CHAPTER I

### Of The Communication, Acceptance And Revocation of Proposals.

3. The communication of proposals, the acceptance of proposals, and the revocation of proposals and acceptance. Communication and revocation of proposals respectively, are deemed to be made by any act or omission of the party proposing, accepting or revoking by which he intends to communicate such proposal, acceptance or revocation, or which has the effect of communicating it.

Communication when complete

4. The communication of a proposal is complete when it comes to the knowledge of the person to whom it is made.

The communication of an acceptance is complete—  
as against the proposer, when it is put into his  
possession to him, so as to be out of the power of the acceptor;  
as against the acceptor, when it comes to the knowledge of the proposer.

The communication of a revocation is complete,—  
as against the person who makes it, when it is put into a  
course of transmission to the person to whom it is made, so as to be out of the power of the person who makes it;  
as against the person to whom it is made, when it comes to his knowledge.

#### *Illustrations.*

(a) A proposes, by letter, to sell a house to B at a certain price.

The communication of the proposal is complete when B receives the letter.

(b) B accepts the proposal by a letter sent by post.

The communication of the acceptance is complete,—

as against A, when the letter is received by A;

as against B, when the letter is received by A.

(c) A revokes his proposal by telegram.

The revocation is complete as against A when the telegram is despatched. It is complete as against B when B receives it.

B revokes his acceptance by telegram. B's revocation is complete as against B when the telegram is despatched, and as against A when it reaches him.

5. A proposal may be revoked at any time before the communication of its acceptance.

Revocation of a proposal and acceptance are complete against the proposer, but not afterwards.

An acceptance may be revoked at any time before the communication of the acceptance is complete as against the acceptor, but not afterwards.

Illustration.

A proposes by a letter sent by post, to sell his house to B.  
B accepts the proposal by a letter sent by post.

A may revoke his proposal at any time before or at the moment when B posts his letter of acceptance, but not afterwards.

B may revoke his acceptance at any time before or at the moment when the letter communicating it reaches A, but not afterwards.

Revocation, how  
made.

6. A proposal is revoked—

- (1) by the communication of notice of revocation by the proposer to the other party;
- (2) by the lapse of the time prescribed in such proposal for its acceptance or, if no time is so prescribed, by the lapse of a reasonable time, without communication of the acceptance;
- (3) by the failure of the acceptor to fulfil a condition precedent to acceptance;
- (4) by the insanity of the acceptor, if the fact of his insanity comes to knowledge of the acceptor after acceptance.

Acceptance must be absolute. In order to convert a proposal into a promise, the acceptance must—

- (1) be absolute and unqualified;
- (2) be expressed in some usual and reasonable manner, unless the proposal prescribes the manner in which it is to be accepted. If the proposal prescribes in a manner in which it is to be accepted, and the acceptance is not made in such manner, the proposer may, within a reasonable time after the acceptance is communicated to him, insist that his proposal shall be accepted in the prescribed manner, and not otherwise; but if he fails to do so, he accepts the acceptance.

8. Rejection of the conditions of a proposal by a person making a proposal or receiving consideration.

Acceptance of any consideration by a proposal which may be offered in response to a proposal, is an acceptance of a proposal.

9. In so far as the proposal or acceptance of any promise is made in words, the promise is said to be express. In so far as such proposal or acceptance is made otherwise than in words, the promise is said to be implied.

## CHAPTER II

### Of Contracts, Voidable Contracts and Void Agreements.

10. All agreements are contracts if they are made by the consent of parties competent to contract, for a lawful consideration and with a lawful object, and are not hereby expressly declared to be void.

What agreements are contracts.

Nothing herein contained shall affect any law in force in British India, and not thereby expressly repealed, by which any contract is required to be made in writing or in the presence of witnesses, or any law relating to the registration of documents.

11. Every person is competent to contract who is of the age of majority according to the law under which he is subject, and who is of sound mind, and is not disqualified from contracting by any law to which he is subject.

What is a sound mind for the purpose of making a contract if, at the time when he makes it, he is capable of understanding and of forming a rational judgment upon its effect upon his interests.

A person who is usually of unsound mind, but occasionally of sound mind, may make a contract when he is of sound mind.

A person who is usually of sound mind, but occasionally of unsound mind, may not make a contract when he is of unsound mind

### *Illustrations*

(a) A patient in a lunatic asylum, who is at intervals of sound mind, may contract during those intervals

(b) A sane man, who is delirious from fever or who is so drunk that he cannot understand the terms of a contract or form a rational judgment as to its effect on his interest, cannot contract whilst such delirium or drunkenness lasts

13 Two or more persons are said to consent when they "Consent" defined agree upon the same thing in the same sense

"Free consent" defined 14 Consent is said to be free when it is not caused by—

- (1) coercion, as defined in section 15, or
- (2) undue influence, as defined in section 16, or
- (3) fraud, as defined in section 17, or
- (4) misrepresentation, as defined in section 18, or
- (5) mistake, subject to the provisions of sections 20, 21 and 22

Consent is said to be so caused when it would not have been given but for the existence of such coercion, undue influence, fraud, misrepresentation or mistake

15 "Coercion" is the committing or threatening to commit, "Coercion" defined any act forbidden by the Indian Penal Code, or the unlawful detaining, or threatening to detain, any property to the prejudice of any person whatever, with the intention of causing any person to enter into an agreement.

*Explanation* —It is immaterial whether the Indian Penal

Code is or is not in force in the place where the contract is employed

### *Illustrations*

A, on board an English ship on the high seas, causes B to enter into an agreement by an act amounting to criminal intemperance under the Indian Penal Code

A afterwards sues B for breach of contract at Calcutta.

A has employed coercion although his act is not an offence by the law of England, and although section 506 of the Indian Penal Code was not in force at the time when or place where the fact was done

16 (1) A contract is said to be induced by "undue influence where the relations subsisting between the parties are such that one of them is in a position to dominate the will of the other and uses that position to obtain an unfair advantage over the other

(2) In particular and without prejudice to the generality of the foregoing principle, a person is deemed to be in a position to dominate the will of another-

(a) where he holds a real or apparent authority over the other, or where he stands in a fiduciary relation to the other, or

(b) where he makes a contract with a person whose mental capacity is temporarily or permanently affected by reason of his illness or mental or bodily distress

(3) Where a person who is in a position to dominate the will of another, enters into a contract with him, and the transaction appears, on the face of it or on the evidence adduced, to be unconscionable, the burden of proving that such contract was not induced by undue influence shall lie upon the person in a position to dominate the will of the other

Nothing in this sub-section shall affect the provisions of section 111 of the Indian Evidence Act, 1872.

### *Illustrations.*

(a) A having advanced money to his son, B, during his minority, upon B's coming of age obtains, by misuse of parental influence a bond from B for a greater amount than the sum due in respect of the advance. A employs undue influence.

(b) A, a man enfeebled by disease or age, is induced by B's influence over him as his medical attendant to agree to pay B an unreasonable sum for his professional services. B employs undue influence.

(c) A, being in debt to B, the money-lender of his village, contracts a fresh loan on terms which appear to be unconscionable. It lies on B to prove that the contract was not induced by undue influence.

(d) A applies to a banker for a loan at a time when there is stringency in the money market. The banker declines to make the loan except at an usually high rate of interest. A accepts the loan on these terms. This is a transaction in the ordinary course of business, and the contract is not induced by undue influence.

17. "Fraud" means and includes any of the following acts committed by a party to a contract, or with "Fraud" defined. his connivance or by his agent, with intent to deceive another party thereto or his agent, or to induce him to enter into the contract :—

- (1) the suggestion as a fact, of that which is not true by one who does not believe it to be true;
- (2) the active concealment of a fact by one having knowledge or belief of the fact;
- (3) a promise made without any intention of performing it;
- (4) any other act fitted to deceive;

- (5) any such act or omission as the law specially designates to be fraudulent.

*Explanation.*—Merely silence as to facts likely to affect the willingness of a person to enter into a contract is not fraud, unless the circumstances of the case are such that, regard being had to them, it is the duty of the person keeping silence to speak, or unless his silence is, in itself, equivalent to speech.

*Illustrations.*

(a) A sells, by auction, to B, a horse which A knows to be unsound. A says nothing to B about the horse's unsoundness. This is not fraud in A.

(b) B is A's daughter and has just come of age. Here, the relation between the parties would make it A's duty to tell B if the horse is unsound.

(c) B says to A—"If you do not deny it, I shall assume that the horse is sound." A says nothing. Here A's silence is equivalent to speech.

(d) A and B, being traders, enter upon a contract. A has private information of a change in prices which would affect B's willingness to proceed with the contract. A is not bound to inform B.

Misrepresentation      18 "Misrepresentation" means and defined. includes—

- (1) the positive assertion, in a manner not warranted by the information of the person making it, of that which is not true, though he believes it to be true;
- (2) any breach of duty which, without an intent to deceive, gains an advantage to the person committing it, or any one claiming under him, misleading another to his prejudice or to the prejudice of any one claiming under him;
- (3) causing however innocently, a party to an agreement to make a mistake as to the substance of the thing which is the subject of the agreement.

**19.** When consent to an agreement is caused by coercion,

\* \* \* \* \*

Voidability of agreements with misrepresentation, the agreement is a contract ~~not~~ ~~voidable~~ contract voidable at the option of the party whose consent was so caused.

A party to a contract, whose consent was caused by fraud or misrepresentation, may, if he thinks fit, insist that the contract shall be performed, and that he shall be put in the position in which he would have been if the representations made had been true.

**Exception.**—If such consent was caused by misrepresentation or by silence, fraudulent within the meaning of section 17, the contract, nevertheless, is not voidable, if the party whose consent was so caused had the means of discovering the truth with ordinary diligence.

**Explanation.**—A fraud or misrepresentation which did not cause the consent to a contract of the party on whom such fraud was practised, or to whom such misrepresentation was made, does not render a contract voidable.

#### *Illustrations.*

(a) A, intending to deceive B, falsely represents that five hundred maunds of indigo are made annually at A's factory, and thereby induces B to buy the factory. The contract is voidable at the option of B.

(b) A, by a misrepresentation, leads B erroneously to believe that five hundred maunds of indigo are made annually at A's factory. B examines the accounts of the factory, which show that only four hundred maunds of indigo have been made. After this B buys the factory. The contract is not voidable on account of A's misrepresentation.

(c) A fraudulently informs B that A's estate is free from incumbrance. B thereupon buys the estate. The estate is subject to a mortgage. B may either avoid the contract, or may insist on its being carried out and the mortgage-debt redeemed.

(d) B, having discovered a vein of ore on the estate of A, adopts means to conceal, and does conceal, the existence of the ore from A. Through A's ignorance B is enabled to buy the estate at an under-value. The contract is voidable at the option of A.

(e) A is entitled to succeed to an estate at the death of B. B dies; C, having received intelligence of B's death, prevents the intelligence reaching A, and thus induces A to sell him his interest in the estate. The sale is voidable at the option of A.

[19A. When consent to an agreement is caused by undue influence, the agreement is a contract voidable at the option of the party whose consent by undue influence was so caused]

Any such contract may be set aside either absolutely or, if the party who was entitled to avoid it has received any benefit thereunder, upon such terms and conditions as to the Court may seem just.

#### *Illustrations:*

(a) A's son has forged B's name to a promissory note. B, under threat of prosecuting A's son obtains bond from A for the amount of the forged note. If B sues on this bond, the Court may set the bond aside.

(b) A, a money-lender, advances Rs. 100 to B, an agriculturist and, by undue influence, induces B to execute a bond for Rs. 200 with interest at 6 per cent per month. The Court may set the bond aside, ordering B to repay the Rs. 100 with such interest as may seem just.

Agreement void  
while both parties  
are under mistake  
as to a matter of  
fact

(c) Where both the parties to an agreement are under a mistake as to a matter of fact essential to the agreement, the agreement is void.

*Explanation*—An erroneous opinion as to the value of the thing which forms the subject-matter of the agreement is not to be deemed a mistake as to a matter of fact.

*Illustrations.*

(a) A agrees to sell to B a specific cargo of goods supposed to be on its way from England to Bombay. It turns out that before the day of the bargain, the ship conveying the cargo had been cast away and the goods lost. Neither party was aware of the facts. The agreement is void.

(b) A agrees to buy from B a certain horse. It turns out that the horse was dead at the time of the bargain, though neither party was aware of the fact. The agreement is void.

(c) A, being entitled to an estate for the life of B, agrees to sell it to C. B was dead at the time of the agreement, but both parties were ignorant of the fact. The agreement is void.

21. A contract is not voidable because it was caused by a mistake as to any law in force in British India, but a mistake as to a law not in force in British India has the same effect as a mistake of fact.

**Effects of mistakes as to law**

[After the establishment of the Federation of India this section applies in relation to Central Acts made for a Federated State as it applies to laws in force in British India.]

*Illustration*

A and B make a contract grounded on the erroneous belief that a particular debt is barred by the Indian Law of Limitation, the contract is not voidable.

**Contract caused by mistake of one party as to a matter of fact**

22 A contract is not voidable merely because it was caused by one of the parties to it being under a mistake as to a matter of fact.

**What considerations and objects are lawful and what not.**

23 The consideration or object of an agreement is lawful, unless—

it is forbidden by law; or  
is of such a nature that, if permitted, it would defeat the provisions of any law; or  
is fraudulent; or

involves or implies injury to the person or property  
or  
the Court regards it as immoral, or opposed to public policy.  
In each of these cases, the consideration or object of an agreement  
is said to be unlawful. Every agreement of which the object  
or consideration is unlawful is void.

*Illustrations.*

(a) A agrees to sell his house to B for 10,000 rupees. Here B's promise to pay the sum of 10,000 rupees is the consideration for A's promise to sell the house, and A's promise to sell the house is the consideration for B's promise to pay the 10,000 rupees. These are lawful considerations.

(b) A promises to pay B 1,000 rupees at the end of six months, if C, who owes that sum to B, fails to pay it. B promises to grant time to C accordingly. Here the promise of each party is the consideration for the promise of the other party and they are lawful considerations.

(c) A promises, for a certain sum paid to him by B, to make good to B the value of his ship if it is wrecked on a certain voyage. Here A's promise is the consideration for B's payment, and B's payment is the consideration for A's promise, and these are lawful considerations.

(d) A promises to maintain B's child and B promises to pay A 1,000 rupees yearly for the purpose. Here the promise of each party is the consideration for the promise of the other party. They are lawful considerations.

(e) A, B and C enter into an agreement for the division among them of gains acquired, or to be acquired, by them by fraud. The agreement is void, as its object is unlawful.

(f) A promises to obtain for B an employment in the public service, and B promises to pay 1,000 rupees to A. The agreement is void, as the consideration for it is unlawful.

(g) A, being agent for a landed proprietor, agrees for money, without the knowledge of his principal, to obtain for B a lease of land belonging to his principal. The agreement between A and

B is void, as it implies a fraud by concealment by A, on his principal.

(k) A promises B to drop a prosecution which he has instituted against B for robbery, and B promises to restore the value of the things taken. The agreement is void, as its object is unlawful.

(l) A's estate is sold for arrears of revenue under the provisions of an Act of the Legislature, by which the defaulter is prohibited from purchasing the estate. B, upon an understanding with A, becomes the purchaser, and agrees to convey the estate to A upon receiving from him the price which B has paid. The agreement is void, as it renders the transaction, in effect, a purchase by the defaulter, and would so defeat the object of the law.

(m) A, who is B's mukhtar, promises to exercise his influence, as such, with B in favour of C, and C promises to pay 1,000 rupees to A. The agreement is void, because it is immoral.

(n) A agrees to let her daughter to hire to B for concubinage. The agreement is void, because it is immoral, though the letting may not be punishable under the Indian Penal Code.

#### **Void Agreements.**

24. If any part of a single consideration for one or more agreements void, if considerations and objects unlawful in part objects, or any one or any one of several considerations for a single object, is unlawful, the agreement is void.

#### *Illustration.*

A promises to superintend, on behalf of B, a legal manufacture of indigo and an illegal traffic in other articles. B promises to pay to A a salary of 10,000 rupees. The agreement is void, the object of A's promise and consideration for B's promise being in part unlawful.

25. An agreement made without consideration is void, unless—

Agreement with out consideration void unless it is in writing and registered.

(1) it is expressed in writing and registered under the law for the time being in force for the registration of [document], and is made on account of natural love and

affection between parties standing in a near relation to each other, or unless

(2) it is a promise to compensate, wholly or in part, a person who has already voluntarily done something for the promisor, or something which the promisor was legally compellable to do, or unless

(3) it is a promise, made in writing and signed by the person or is a promise to be charged therewith, or by his agent generally or specially authorized in that behalf, to pay wholly or in part a debt of which the creditor might have enforced payment but for the law, for the limitation of suits.

In any of these cases, such an agreement is a contract.

*Explanation 1.*—Nothing in this section shall affect the validity, as between the donor and donee, of any gift actually made.

*Explanation 2.*—An agreement to which the consent of the promisor is freely given is not void merely because the consideration is inadequate; but the inadequacy of the consideration may be taken into account by the Court in determining the question whether the consent of the promisor was freely given.

#### *Illustrations.*

(a) A promises, for no consideration, to give to B Rs. 1,000. This is a void agreement.

(b) A, for natural love and affection, promises to give his son, B, Rs. 1,000. A puts his promise to B into writing and registers it. This is a contract.

(c) A finds B's purse and gives it to him. B promises to give A Rs. 50. This is a contract.

(d) A supports B's infant son. B promises to pay A's expenses in so doing. This is a contract.

(e) A owes B Rs. 1,000, but the debt is barred by the Limitation Act. A signs a written promise to pay B Rs. 500 on account of the debt. This is a contract.

(f) A agrees to sell a horse worth Rs. 1,000 for Rs. 10. A's consent to the agreement was freely given. The agreement is a contract notwithstanding the inadequacy of the consideration.

(g) A agrees to sell a horse worth Rs. 1,000 for Rs. 10. A denies that his consent to the agreement was freely given.

The inadequacy of the consideration is a fact which the Court should take into account in considering whether or not A's consent was freely given.

*Agreement in restraint or marriage void* 26. Every agreement in restraint of the marriage of any person, other than a minor, is void

*Agreement in restraint of trade void* 27. Every agreement by which any one is restrained from exercising a lawful profession, trade or business of any kind, is to that extent void.

*Exception 1.*—One who sells the good-will of a business may agree with the buyer to refrain from carrying on a similar business, *Saving of agreement not to carry on business of which good-will is sold.* within specified local limits, so long as the buyer, or any person deriving title to the good-will from him, carries on a like business therein. Provided that such limits appear to the Court reasonable regard being had to the nature of the business.

*Agreements in restraint of legal proceedings void* 28. Every agreement, by which any party thereto is restricted absolutely from enforcing his rights under or in respect of any contract, by the usual legal proceedings in the ordinary tribunals, or which limits the time within which he may thus enforce his rights, is void to that extent.

*Savings of contract to refer to arbitration dispute that may arise* *Exception 1.*—This section shall not render illegal a contract by which two or more persons agree that any dispute which may arise between them in respect of any subject or class of subjects shall be referred to arbitration, and that only the amount awarded in

such arbitration shall be recoverable in respect of the dispute so referred.

*When such a contract has been made, a suit may be brought for its specific performance, and if a suit, other than for such specific performance, or for the recovery of the amount so awarded, is brought by one party to such contract against any other such party in respect of any subject which they have so agreed to refer, the existence of such contract shall be a bar to the suit.*

*Exception 2.—Nor shall this section render illegal any contract in writing, by which two or more persons agree to refer to arbitration any question between them which has already arisen, or affect any provision of any law in force for the time being as to references to arbitration.*

*Agreement void for uncertainty* 29. Agreements, the meaning of which is not certain, or capable of being made certain, are void.

#### *Illustrations.*

(a) A agrees to sell to B "a hundred tons of oil." There is nothing whatever to show what kind of oil was intended. The agreement is void for uncertainty.

(b) A agrees to sell to B one hundred tons of oil of a specified description, known as an article of commerce. There is no uncertainty here to make the agreement void.

(c) A, who is a dealer in cocoanut-oil only, agrees to sell to B "one hundred tons oil." The nature of A's trade affords an indication of the meaning of the words, and A has entered into a contract for the sale of one hundred ton, of cocoanut-oil.

(d) A agrees to sell to B "all the grain in my granary at Ramnagar." There is no uncertainty here to make the agreement void.

(e) A agrees to sell to B "one thousand maunds of rice at a price to be fixed by C." As the price is capable of being made certain, there is no uncertainty here to make the agreement void.

(f) A agrees to sell to B "my white horse for rupees five hundred or rupees one thousand." There is nothing to show which of the two prices was to be given. The agreement is void.

**30. Agreements by way of wager are void; and no suit shall be brought for recovering anything alleged to be won on any wager, or entrusted to any person to abide the result of any game or other uncertain event on which any wager is made.**

**Exception in favour of certain prizes for horse racing.** This section shall not be deemed to render unlawful a subscription, or contribution, or agreement to subscribe or contribute, made or entered into for or toward any plate, prize or sum of money, of the value or amount of five hundred rupees or upwards, to be awarded to the winner or winners of any horse-race.

**Section 294A of the Indian Penal Code not affected.** Nothing in this section shall be deemed to legalize any transaction connected with horse-racing, to which the provisions of section 294 of the Indian Penal Code apply.

### CHAPTER III

#### Of Contingent Contracts.

**31. A "contingent contract"** is a contract to do or not to do something, if some event, collateral to such contract, does or does not happen.

#### *Illustration.*

A contracts to pay B R<sup>०</sup> 10,000 if B's house is burnt. This is a contingent contract.

**Enforcement of contracts contingent on an event happening.** Contingent contracts to do or not to do anything if an uncertain future event happens cannot be enforced by law unless and until that event has happened.

If the event becomes impossible such contracts become void.

*Illustrations.*

(a) A makes a contract with B to buy B's horse if A survives C. This contract cannot be enforced by law unless and until C dies in A's lifetime.

(b) A makes a contract with B to sell a horse to B at a specified price, if C, to whom the horse has been offered, refuses to buy him. The contract cannot be enforced by law unless and until C refuses to buy the horse.

(c) A contracts to pay B a sum of money when B marries C. C dies without being married to B. The contract becomes void.

33. Contingent contracts to do or not to do anything if an uncertain future event does not happen can be enforced when the happening of that event becomes impossible, and not before.

*Illustration.*

A agrees to pay B a sum of money if a certain ship does not return. The ship is sunk. The contract can be enforced when the ship sinks.

34. If the future event on which a contract is contingent is the way in which a person will act at an unspecified time, the event shall be considered to become impossible when such person does anything which renders it impossible that he should so act within any definite time, or when event on which contract is contingent to be deemed impossible, if it is the future conduct of a living person.

otherwise than under further contingencies.

*Illustration.*

A agrees to pay B a sum of money if B marries C.

C marries D. The marriage of B to C must now be considered impossible, although it is possible that D may die and that C may afterwards marry B.

**35. Contingent contracts to do or not to do anything if a specified uncertain event happens within a fixed time**

When contracts become void which are contingent on happening of specified event within fixed time.

Contingent contracts to do or not to do anything if a specified uncertain event does not happen within a fixed time

When contracts may be enforced which are contingent on specified event not happening within fixed time.

will not happen.

*Illustrations*

(a) A promises to pay B a sum of money if a certain ship returns within a year. The contract may be enforced if the ship returns within the year, and becomes void if the ship is burnt within the year.

(b) A promises to pay B a sum of money if a certain ship does not return within a year. The contract may be enforced if the ship does not return within the year, or is burnt within the year.

**36. Contingent agreements to do or not to do anything, if an impossible event happens, are void, whether the impossibility of the event is known or not to the parties to the agreement at the time when it is made.**

*Illustrations.*

(a) A agrees to pay B 1,000 rupees if two straight lines should enclose a space. The agreement is void.

(b) A agrees to pay B 1,000 rupees if B will marry A's daughter C. C was dead at the time of agreement. The agreement is void.

## CHAPTER IV

### Of the Performance of Contracts.

#### *Contracts which must be performed.*

37. The parties to a contract must either perform, or offer to perform their respective promises unless such performance is dispensed with or excused under the provisions of this Act, or of any other law.

Promises bind the representatives of the promisors in case of the death of such promisors before performance, unless a contrary intention appears from the contract.

#### *Illustrations.*

(a) A promises to deliver goods to B on a certain day on payment of Rs. 1,000. A dies before that day. A's representatives are bound to deliver the goods to B, and B is bound to pay the Rs. 1,000 to A's representatives.

(b) A promises to paint a picture for B by a certain day, at a certain price. A dies before the day. The contract cannot be enforced either by A's representatives or by B.

38. Where a promisor has made an offer of performance to the promisee, and the offer has not been accepted, the promisor is not responsible for non performance, nor does he thereby lose his rights under the contract.

Every such offer must fulfil the following conditions :—

(1) it must be unconditional :

(2) it must be made at a proper time and place, and under such circumstances that the person to whom it is made may have a reasonable opportunity of ascertaining that the person by whom it is made is able and willing there and then to do the whole of what he is bound by his promise to do :

(3) if the offer is an offer to deliver anything to the promisee the promisee must have a reasonable opportunity of seeing that the thing offered is the thing which the promisor is bound by his promise to deliver.

An offer to one of several joint promisees has the same legal consequences as an offer to all of them.

#### *Illustration.*

A contracts to deliver to B at his warehouse, on the first March, 1873, 100 bales of cotton of a particular quality. In order to make an offer of a performance with the effect stated in this section, A must bring the cotton to B's warehouse, on the appointed day, under such circumstances that B may have a reasonable opportunity of satisfying himself that the thing offered is cotton of the quality contracted for, and that there are 100 bales.

39. When a party to a contract has refused to perform, or disabled himself from performing, his promise in its entirety, the promisee may put an end to the contract, unless he has signified by words or conduct, his acquiescence in its continuance.

*Effect of refusal of party to perform promise wholly.*

#### *Illustrations.*

(a) A, a singer, enters into a contract with B, the manager of a theatre, to sing at his theatre two nights in every week during the next two months. And B engages to pay her 100 rupees for each night's performance. On the sixth night A wilfully absents herself from the theatre. B is at liberty to put an end to the contract.

(b) A, a singer, enters into a contract with B, the manager of a theatre, to sing at his theatre two nights in every week during the next two months, and B engages to pay her at the rate of 100 rupees for each night. On the sixth night A wilfully absents herself. With the assent of B, A sings on the seventh night. B has signified his acquiescence of the contract, and

cannot now put an end to it but is entitled to compensation for the damage sustained by him through A's failure to sing on the sixth night.

*By whom Contracts must be performed.*

- 40 If it appears from the nature of the case that it was the intention of the parties to any contract that any promise contained in it should be performed by the promisor himself, such promise must be performed by the promisor. In other cases, the promisor or his representatives may employ a competent person to perform it

*Illustrations:*

(a) A promises to pay B a sum of money. A may perform this promise, either by personally paying the money to B or by causing it to be paid to B by another; and, if A dies before the time appointed for payment, his representatives must perform the promise, or employ some proper person to do so.

(b) A promises to paint a picture for B. A must perform this promise personally.

Effect of accepting performance from third person  
41 When a promisee accepts performance of the promise from a third person, he cannot afterwards enforce it against the promisor.

Devolution of joint liabilities  
42 When two or more persons have made a joint promise, then unless a contrary intention appears by the contract all such persons, during their joint lives, and after the death of any of them, his representatives jointly with the survivor or survivors, and after the death of the last survivor, the representatives of all jointly, must fulfil the promise.

Any one of joint promisors may be compelled to perform  
43 When two or more persons make a joint promise, the promisee may, in the absence of express agreement to the contrary, compel any [one or more] of such joint promisors to perform the whole of the promise.

**Each of two or more joint promisors may compel every other joint promisor to contribute equally**

**Each promisor may compel contribution.** with himself to the performance of the promise, unless a contrary intention appears from the contract.

**If any one of two or more joint promisors makes default in such contribution, the remaining joint**

**Sharing of loss by default in contribution.** promisors must bear the loss arising from such default in equal shares.

**Explanation.—**Nothing in this section shall prevent a surety from recovering from his principal, payments made by the surety on behalf of the principal, or entitle the principal to recover anything from the surety on account of payments made by the principal.

#### *Illustrations.*

(a) A, B and C jointly promise to pay D 3,000 rupees. D may compel either A or B or C to pay him 3,000 rupees.

(b) A, B and C jointly promise to pay D the sum of 3,000 rupees. C is compelled to pay the whole. A is insolvent but his assets are sufficient to pay one-half of his debts. C is entitled to receive 500 rupees from A's estate, and 1,250 rupees from B.

(c) A, B and C are under a joint promise to pay D 3,000 rupees. C is unable to pay anything, and A is compelled to pay the whole. A is entitled to receive 1,500 rupees from B.

(d) A, B and C are under a joint promise to pay D 3,000 rupees. A and B being only sureties for C. C fails to pay. A and B are compelled to pay the whole sum. They are entitled to recover it from C.

**44. Where two or more persons have made a joint promise, a release of one of such joint promisors by Effect of release of the promisee does not discharge the other one joint promisor joint promisor or joint promisors: neither does it free the joint promisor so released from responsibility to the other joint promisor or joint promisors.**

**45.** When a person has made a promise to two or more persons jointly, then, unless a contrary Devolution of joint intention appears from the contract, the rights right to claim performance rests, is between him and them, with them during their joint lives, and, after the death of any of them, with the representative of such deceased person jointly with the survivor or survivors and, after the death of the last survivor, with the representatives of all jointly

#### *Illustration*

A, in consideration of 5,000 rupees lent to him by B and C, promises B and C jointly to repay them that sum with interest on a day specified. B dies. The right to claim performance rests with B's representative jointly with C during C's life, and after the death of C with the representatives of B and C jointly

#### *Time and place for performance*

**46.** Where by the contract a promisor is to perform his promise without application by the promisee and no time for performance is specified the engagement must be performed within a reasonable time

*Explanation* The question what is reasonable time is in this particular case a question of fact

**47.** When a promise is to be performed on a certain day, and the time and place for performance of promise where time is specified and no application to be made it without application by the promisee, the promisee may perform it in time during the usual hours of business on such day and at the place at which the promise ought to be performed

#### *Illustration*

A promises to deliver goods at B's warehouse on the first January. On that day A brings the goods to B's warehouse, but after the usual hour for closing it, and they are not received. A has not performed his promise

48. When a promise is to be performed on a certain day, and the promisor has not undertaken to perform it without application by the promisee, it is the duty of the promisee to apply for performance at a proper place and within the usual hours of business.

**Application for performance on certain day to be at proper time and place.**

*Explanation.*—The question "what is a proper time and place" is, in each particular case, a question of fact.

49. When a promise is to be performed without application by the promisee, and no place is fixed for the performance of it, it is the duty of the promisor to apply to the promisee to appoint a reasonable place for the performance of the promise, and to perform it at such place.

**Place for performance of promise where no application to be made and no place fixed for performance.**

A undertakes to deliver a thousand maunds of jute to B on a fixed day. A must apply to B to appoint a reasonable place for the purpose of receiving it, and must deliver it to him at such place.

**Performance in manner or at times prescribed or sanctioned by promisee.**

50. The performance of any promise may be made in any manner, or at any time which the promisee prescribes or sanctions.

#### *Illustrations.*

(a) B owes A 2,000 rupees. A desires B to pay the amount to A's account with C, a banker. B, who also banks with C, orders the amount to be transferred from his account to A's credit and this is done by C. Afterwards, and before A knows of the transfer, C fails. There has been a good payment by B.

(b) A and B are mutually indebted. A and B settle an account by setting off one item against another, and B pays A the balance found to be due from him upon such settlement. This amounts to a payment by A and B respectively, of the sums which they owed to each other.

(c) A owes B 2,000 rupees. B accepts some of A's goods in deduction of the debt. The delivery of the goods operates as a part payment.

(d) A desires B, who owes him Rs. 100, to send him a note for Rs. 100 by post. The debt is discharged as soon as B puts into the post a letter containing the notes duly addressed to A.

### *Performance of Reciprocal Promises.*

Promisor not bound to perform unless reciprocal promisee ready and willing to perform.

51. When a contract consists of reciprocal promises to be simultaneously performed, no promisor need perform his promise unless the promisee is ready and willing to perform his reciprocal promise.

### *Illustrations.*

(a) A and B contract that A shall deliver goods to B to be paid for by B on delivery.

A need not deliver the goods, unless B is ready and willing to pay for the goods on delivery.

B need not pay for the goods, unless A is ready and willing to deliver them on payment.

(b) A and B contract that A shall deliver goods to B at a price to be paid by instalments, the first instalment to be paid on delivery.

A need not deliver, unless B is ready and willing to pay the first instalment on delivery.

B need not pay the first instalment unless A is ready and willing to deliver the goods on payment of the first instalment.

52. Where the order in which reciprocal promises are to be performed is expressly fixed by the contract, they shall be performed in that order ; and, where the order is not expressly fixed by the contract, they shall be performed in that order which the nature of the transaction requires.

Order of performance of reciprocal promises.

*Illustrations.*

(a) A and B contract that A shall build a house for B at a fixed price. A's promise to build the house must be performed before B's promise to pay for it.

(b) A and B contract that A shall make over his stock-in-trade to B at a fixed price, and B promises to give security for the payment of the money. A's promise need not be performed until the security given, for the nature of transaction requires thus A should have security before he delivers up his stock.

53. When a contract contains reciprocal promises, and one party to the contract prevents the other from performing his

*Liability of party preventing event on which contract is to take effect.* promise, the contract becomes voidable at the option of the party so prevented : and he is entitled to compensation from the other party for any loss which he may sustain in consequence of the non-performance of the contract.

*Illustration.*

A and B contract that B shall execute certain work for A for a thousand rupees. B is ready and willing to execute the work accordingly, but A prevents him from doing so. The contract is voidable at the option of A ; and, if he elects to rescind it, he is entitled to recover from A compensation for any loss which he has incurred by its non-performance.

54. When a contract consists of reciprocal promises, such that one of them cannot be performed, or that its performance

*Effect of default as formed in contract consisting of reciprocal promises.* cannot be claimed till the other has been performed, and the promisor of the promise which last mentioned fails to perform it, such promisor cannot claim the performance of the reciprocal promise, and must make compensation to the other party to the contract for any loss which such other party may sustain by the non-performance of the contract.

*Illustrations*

(a) A hires B's ship to take in and convey iron from Calcutta to the Mauritius, a cargo to be provided by A. B receiving a certain freight for its conveyance. A does not provide any cargo for the ship. A cannot claim the performance of B's promise and must make compensation to B for the loss which B sustains by the non performance of the contract.

(b) A contracts with B to execute certain builder's work for a fixed price. B supplying the scaffolding and timber necessary for the work. B refuses to furnish any scaffolding or timber, and the work cannot be executed. A need not execute the work, and B is bound to make compensation to A for any loss caused to him by the non performance of the contract.

(c) A contracts with B to deliver to him at a specified place, certain merchandise on board a ship which cannot arrive for a month, and B engages to pay for the merchandise within a week from the date of the contract. B does not pay within the week. A's promise to deliver need not be performed and B must make compensation.

(d) A promises B to sell him one hundred bales of merchandise to be delivered next day and B promises A to pay for them within a month. A does not deliver according to his promise. B's promise to pay need not be performed and A must make compensation.

55 When a party to a contract promises to do a certain thing at or before a specified time or certain things at or before a specified time, and fails to do any such thing

*Effect of failure to* do it or before the specified time, the performance at fixed time contract in which time is essential performed becomes voidable at the option of the promisee if the intention of the parties was that time should be of the essence of the contract.

If it was not the intention of the parties that time should be of the essence of the contract, the contract

**Effect of such failure when time is not essential.** does not become voidable by the failure to do such thing at or before the specified time but the promisee is entitled to compensation from the promisor for any loss occasioned to him by such failure.

If, in case of a contract voidable on account of the promisor's failure to perform his promise at the time agreed,

**Effect of acceptance of performance at time other than that agreed upon.** the promisee accepts performance of such promise at any time other than that agreed, the promisee cannot claim compensation for any loss occasioned by the non-performance of the promise at the time agreed, unless, at the time of such acceptance, he gives notice to the promisor of his intention to do so.

**Agreement to do impossible act.** 56 An agreement to do an act impossible in itself is void.

A contract to do an act which, after the contract is made, becomes impossible, or, by reason of some

**Contract to do act afterwards becoming impossible or unlawful.** event which the promisor could not prevent, unlawful, becomes void when the act becomes impossible or unlawful.

Where one person has promised to do something which he knew, or, with reasonable diligence, might have known, and which the promisee did not

**Compensation for loss through non-performance of act known to be impossible or unlawful.** know to be impossible or unlawful, such promisor must make compensation to such promisee for any loss which such promisee sustains through the non-performance of the promise.

#### *Illustrations.*

(a) A agrees with B to discover treasure by magic. The agreement is void.

(b) A and B contract to marry each other. Before the time fixed for the marriage, A goes mad. The contract becomes void.

(c) A contracts to marry B, being already married to C, and being forbidden by the law to which he is subject to practise polygamy. A must make compensation to B for the loss caused to her by the non-performance of his promise.

(d) A contracts to take in cargo for B at a foreign port. A's Government afterwards declares war against the country in which the port is situated. The contract becomes void when war is declared.

(e) A contracts to act at a theatre for six months in consideration of a sum paid in advance by B. On several occasions A is too ill to act. The contract to act on those occasions becomes void.

57. Where persons reciprocally promise, firstly, to do certain reciprocal promises things which are legal, and, secondly, under to do things legal and also other things specified circumstances, to do certain other illegal things which are illegal, the first set of promises is a contract, but the second is a void agreement.

*Illustration.*

A and B agree that A shall sell B a house for 10,000 rupees, but that, if B uses it as a gambling house, he shall pay A 50,000 rupees for it.

The first set of reciprocal promises, namely, to sell the house and to pay 10,000 rupees for it, is a contract.

The second set is for an unlawful object, namely, that B may use the house as a gambling house, and is a void agreement.

58. In the case of an alternative promise, one branch of Alternative promise, which is legal and the other illegal, the legal one branch being branch alone can be enforced.

*Illustration*

A and B agree that A shall pay B 1,000 rupees, for which B shall afterwards deliver to A either rice or smuggled opium.

This is a valid contract to deliver rice and void agreement as to the opium.

*Appropriation of Payments.*

59. Where a debtor owing several distinct debts to one person, makes a payment to him, either

Application of payment where debt to be discharged is indicated. with express intimation, or under circumstances implying that the payment is to be applied to the discharge of some particular debt, the payment, if accepted, must be applied accordingly.

*Illustrations.*

(a) A owes to B, among other debts, 1,000 rupees upon a promissory note which falls due on the first June. He owes B no other debt of that amount. On the first June A pays to B 1,000 rupees. The payment is to be applied to the discharge of the promissory note.

(b) A owes to B among other debts, the sum of 567 rupees. B writes to A and demands payment of this sum. A sends to B 567 rupees. This payment is to be applied to the discharge of the debt of which B had demanded payment.

60. Where the debtor has omitted to intimate and there are no other circumstances indicating to which

Application of payment where debt to be discharged is not indicated. debt the payment is to be applied, the creditor may apply it at his discretion to any lawful debt actually due and payable to him from the debtor, whether its recovery is or is not barred by the law in force for the time being as to the limitation of suits.

61. Where neither party makes any appropriation, the payment shall be applied in discharge of the

Application of payment where neither party appropriates. debts in order of time, whether they are or are not barred by the law in force for the time being as to the limitation of suits.

If the debts are of equal standing, the payment shall be applied in discharge of each proportionably.

*Contracts which need not be performed.*

**Effect of novation, rescission and alteration of contract.** 62. If the parties to a contract agree to substitute a new contract for it, or to rescind or alter it, the original contract need not be performed.

*Illustrations.*

(a) A owes money to B under a contract. It is agreed between A, B and C that B shall thenceforth accept C as his debtor, instead of A. The old debt of A to B is at an end, a new debt from C to B has been contracted.

(b) A owes B 10,000 rupees. A enters into an arrangement with B, and gives B a mortgage of his (A's) estate for 5,000 rupees in place of the debt of 10,000 rupees. This is a new contract and extinguishes the old.

(c) A owes B 1,000 rupees under a contract. B owes C 1,000 rupees. B orders A to credit C with 1,000 rupees in his books, but C does not assent to the arrangement. B still owes C 1,000 rupees, and no new contract has been entered into.

63. Every promisee may dispense with or remit, wholly or in part, the performance of the promise made to him, or may extend the time for such performance, or may accept instead of it any satisfaction which he thinks fit.

*Illustrations.*

(a) A promises to paint a picture for B. B afterwards forbids him to do so. A is no longer bound to perform the promise.

(b) A owes B 5,000 rupees. A pays to B, and B accepts in satisfaction of the whole debt 2,000 rupees paid at the time and place at which the 5,000 rupees were payable. The whole debt is discharged.

(c) A owes to B 5,000 rupees. C pays to B 1,000 rupees,

and B accepts them, in satisfaction of his claim on A. This payment is a discharge of the whole claim.

(d) A owes B under a contract, a sum of money, the amount of which has not been ascertained. A without ascertaining the amount gives to B, and B, in satisfaction thereof, accepts, the sum of 2,000 rupees. This is a discharge of the whole debt whatever may be its amount.

(e) A owes B 2,000 rupees, and is also indebted to other creditors. A makes an arrangement with his creditors, including B, to pay them a [composition] of eight annas in the rupee upon their respective demands. Payment to B of 1,000 rupees is a discharge of B's demand.

(f) When a person at whose option a contract is voidable rescinds it, the other party thereto need not perform any promise therein contained in which he is promisor.

**Consequences of rescission of voidable contract** The party rescinding a voidable contract shall, if he has received any benefit thereunder from another party to such contract, restore such benefit, so far as may be, to the person from whom it was received.

(g) When agreement is discovered to be void, or when a contract becomes void, any person who has received any advantage under such agreement or contract is bound to restore it or to make compensation for it, to the person from whom he received it.

#### Illustrations:

(a) A pays B 1,000 rupees in consideration of B's promise, to marry C, A's daughter. C is dead at the time of the promise. The agreement is void, but B must repay A the 1,000 rupees.

(b) A contracts with B to deliver to him 250 maunds of rice before the first of May. A delivers 130 maunds only before that day, and none after. B retains the 130 maunds after the first of May. He is bound to pay A for them.

(c) A, a singer, contracts with B, the manager of a theatre,

to sing at his theatre for two nights in every week during the next two months, and B engages to pay her a hundred rupees for each night's performance. On the sixth night, A wilfully absents herself from the theatre, and B, in consequence, rescinds the contract. B must pay A for the five nights on which she had sung.

(d) A contracts to sing for B at a concert for 1,000 rupees, which are paid in advance. A is too ill to sing. A is not bound to make compensation to B for the loss of the profits which B would have made if A had been able to sing, but must refund to B the 1,000 rupees paid in advance.

Mode of communicating or revoking  
rescission of voidable  
contract.

66. The rescission of a voidable contract may be communicated or revoked in the same manner, and subject to the same rules, as apply to the communication or revocation of a proposal.

Effect of neglect of  
promisee to afford  
promisor reasonable  
facilities for perform-

67. If any promisee neglects or refuses to afford the promisor reasonable facilities for the performance of his promise, the promisor is excused by such neglect or refusal as to any non-performance caused thereby.

#### *Illustration.*

A contracts with B to repair B's house.

B neglects or refuses to point out to A the places, in which his house requires repair.

A is excused for the non-performance of the contract if it is caused by such neglect or refusal.

## CHAPTER V

### Of certain Relations resembling those created by Contract.

68. If a person, incapable of entering into a contract, or any one whom he is legally bound to support is

Claim for necessities supplied to person incapable of contracting, or on his account who has furnished such supplies is entitled to be reimbursed from the property of such incapable person.

#### *Illustrations.*

(a) A supplies B, a lunatic, with necessities suitable to his condition in life. A is entitled to be reimbursed from B's property.

(b) A supplies the wife and children of B, a lunatic, with necessities suitable to their condition in life. A is entitled to be reimbursed from B's property.

Reimbursement of payment of money which another is bound due by another in payment of which he is interested by law to pay, and who therefore pays it, is entitled to be reimbursed by the other

#### *Illustration.*

B holds land in Bengal, on a lease granted by A, the zemindar. The revenue payable by A to the Government being in arrear, his land is advertised for sale by the Government. Under the revenue law, the consequence of such sale will be the annulment of B's lease. B, to prevent the sale and the consequent annulment of his own lease, pays to the Government the sum due from A. A is bound to make good to B the amount so paid

70. Where a person lawfully does anything for another person, or delivers anything to him, not in

Obligation of person enjoying benefit of non-gratuitous act tending to do so gratuitously, and such other person enjoys the benefit thereon, the latter is bound to make compensation to the former in respect of, or to restore, the thing so done or delivered

*Illustrations.*

(a) A, a tradesman, leaves goods at B's house by mistake. B treats the goods as his own. He is bound to pay A for them.

(b) A saves B's property from fire. A is not entitled to compensation from B, if the circumstances show that he intended to act gratuitously.

Responsibility  
finder of goods.

71. A person who finds goods belonging to another and takes them into his custody, is subject to the same responsibility as a bailee.

Liability of person  
to whom money is  
paid, or thing deli-  
vered, by mistake or  
under coercion.

72. A person to whom money has been paid, or anything delivered by mistake or under coercion, must repay or return it.

*Illustrations.*

(a) A and B jointly owe 100 rupees to C. A alone pays the amount to C, and B, not knowing this fact, pays 100 rupees over again to C. C is bound to repay the amount to B.

(b) A railway company refuses to deliver up certain goods to the consigner, except upon the payment of an illegal charge for carriage. The consignee pays the sum charged in order to obtain the goods. He is entitled to recover so much of the charge as was illegally excessive.

## CHAPTER VI.

## Of the Consequences of Breach of Contract.

73. When a contract has been broken, the party who suffers by such breach is entitled to receive from the party who has

broken the contract, compensation for any loss or damage caused by breach of contract, which naturally arose in the usual course of things from such breach, or which the parties knew, when they made the contract, to be likely to result from the breach of it.

Such compensation is not to be given for any remote and indirect loss or damage sustained by reason of the breach.

When an obligation resembling those created by contract has been incurred and has not been discharged, Compensation for failure to discharge any person injured by the failure to discharge it is entitled to receive the same obligation resembling those created by contract. compensation from the party in default, as if such person had contracted to discharge it and had broken his contract.

*Explanation.*—In estimating the loss or damage arising from a breach of contract, the means which existed of remedying the inconvenience caused by the non-performance of the contract must be taken into account.

#### *Illustrations.*

(a) A contracts to sell and deliver 50 maunds of saltpetre to B, at a certain price to be paid on delivery. A breaks his promise. B is entitled to receive from A, by way of compensation, the sum, if any, by which the contract price falls short of the price for which B might have obtained 50 maunds of saltpetre of like quality at the time when the saltpetre ought to have been delivered.

(b) A hires B's ship to go to Bombay, and there takes on board, on the first of January, a cargo which A is to provide and to bring it to Calcutta, the freight to be paid when earned. B's ship does not go to Bombay, but A has opportunities of procuring suitable conveyance for the cargo upon terms as advantageous as those on which he had chartered the ship. A avails himself of those opportunities, but is put to trouble and expense in doing so. A is entitled to receive compensation from B in respect of such trouble and expense.

(c) A contracts to buy of B, at a stated price, 50 maunds of rice, no time being fixed for delivery. A afterwards informs B that he will not accept the rice if tendered to him. B is entitled to receive from A, by way of compensation, the amount, if any, by which the contract price exceeds that which B can obtain for the rice at the time when A informs B that he will not accept it.

(d) A contracts to buy B's ship for 50,000 rupees, but breaks his promise. A must pay to B, by way of compensation, the excess, if any, of the contract price over the price which B can obtain for the ship at the time of the breach of promise.

(e) A, the owner of a boat, contracts with B to take a cargo of jute to Mirzapur, for sale at that place, starting on a specified day. The boat, owing to some avoidable cause does not start at the time appointed, whereby the arrival of the cargo at Mirzapur is delayed beyond the time when it would have arrived if the boat had sailed according to the contract. After that date, and before the arrival of the cargo, the price of jute falls. The measure of the compensation payable to B by A is the difference between the price which B could have obtained for the cargo at Mirzapur at the time when it would have arrived if forwarded in due course and its market price at the time when it actually arrived.

(f) A contracts to repair B's house in certain manner, and receives payment in advance. A repairs the house, but not according to contract. B is entitled to recover from A the cost of making the repairs conform to the contract.

(g) A contracts to let his ship to B for 1 year, from the first of January, for a certain price. Freight rises, and on the first of January the hire obtainable for the ship is higher than the contract price. A breaks his promise. He must pay to B, by way of compensation, a sum equal to the difference between the contract price and the price for which B could hire a similar ship for 1 year on and from the first of January.

(h) A contracts to supply B with a certain quantity of iron at fixed price, being a higher price than that for which B could procure and deliver the iron. B wrongfully refuses to receive the iron. B must pay to A, by way of compensation, the difference between the contract price of the iron and the sum for which A could have obtained and delivered it.

(i) A delivers to B, a common cutter, a machine to be conveyed, without delay, to A's mill, informing B that his mill is stopped for want of the machine. B unreasonably delays the

delivery of the machine, and A, in consequence, loses a profitable contract with the Government. A is entitled to receive from B, by way of compensation, the average amount of profit which would have been made by the working of the mill during the time that delivery of it was delayed, but not the loss sustained through the loss of the Government contract.

(j) A, having contracted with B to supply B with 1,000 tons of iron at 100 rupees a ton, to be delivered at a stated time, contracts with C for the purchase of 1,000 tons of iron at 90 rupees a ton, telling C that he does so for the purpose of performing his contract with B. C fails to perform his contract with A, who cannot procure other iron, and B, in consequence, rescinds the contract. C must pay to A 20,000 rupees, being the profit which A would have made by the performance of his contract with B.

(k) A contracts with B to make and deliver to B, by a fixed day, for a specified price, a certain piece of machinery. A does not deliver the piece of machinery at the time specified, and, in consequence of this, B is obliged to procure another at a higher price than that which he was to have paid to A, and is prevented from performing a contract which B had made with a third person at the time of his contract with A (but which had not been then communicated to A), and is compelled to make compensation for breach of that contract. A must pay to B, by way of compensation, the difference between the contract price of the piece of machinery and the sum paid by B for another, but not the sum paid by B to the third person by way of compensation.

(l) A, a builder, contracts to erect and finish a house by the first of January, in order that B may give possession of it at that time to C, to whom B has contracted to let it. A is informed of the contract between B and C. A builds the house so badly that, before the first of January, it falls down and has to be re-built by B, who, in consequence loses the rent which he was to have received from C, and is obliged to make compensation to C for the breach of his contract. A must make compensation to B for the cost of re-building the house for the rent lost, and for the compensation made to C.

(m) A sells certain merchandise to B, warranting it to be of a particular quality, and B, in reliance upon this warranty, sells it to C with a similar warranty. The goods prove to be not according to the warranty, and B becomes liable to pay C a sum of money by way of compensation. B is entitled to be reimbursed this sum by A.

(n) A contracts to pay a sum of money to B on a day specified. A does not pay the money on that day. B in consequence of not receiving the money on that day is unable to pay his debts, and is totally ruined. A is not liable to make good to B anything except the principal sum he contracted to pay, together with interest up to the day of payment.

(o) A contracts to deliver 50 maunds of saltpetre to B on the first of January, at a certain price. B afterwards, before the first of January, contracts to sell the saltpetre to C at a price higher than the market price of the first of January. A breaks his promise. In estimating the compensation payable by A to B, the market price of the first of January, and not the profit which would have accrued to B from the sale to C, is to be taken into account.

(p) A contracts to sell and deliver 500 bales of cotton to B on a fixed day. A knows nothing of B's mode of conducting his business. A breaks his promise, and B, having no cotton, is obliged to close his mill. A is not responsible to B for the loss caused to B by the closing of the mill.

(q) A contracts to sell and deliver to B, on the first of January, certain cloth which B intends to manufacture into caps of a particular kind, for which there is no demand, except at that season. The cloth is not delivered till after the appointed time, and too late to be used that year in making caps. B is entitled to receive from A, by way of compensation, the difference between the contract price of the cloth and its market price at the time of delivery, but not the profits which he expected to obtain by making caps, nor the expenses which he has been put to in making preparation for the manufacture.

(i) A, a ship-owner, contracts with B to convey him from Calcutta to Sydney in A's ship, sailing on the first of January and B pays to A, by way of deposit one-half of his passage-money. The ship does not sail on the first of January, and B, after being, in consequence, detained in Calcutta for some time, and thereby put to some expense, proceeds to Sydney in another vessel, and, in consequence, arriving too late in Sydney, loses a sum of money A is liable to repay to B his deposit, with interest, and the expense to which he is put by his detention in Calcutta, and the excess, if any, of the passage-money paid for the second ship over that agreed upon for the first, but not the sum of money which B lost by arriving in Sydney too late.

74 | When a contract has been broken, if a sum is named in the contract as the amount to be paid in case of such breach, compensation for or if the contract contains any other breach of contract stipulation by way of penalty, the party where penalty stipula complaining of the breach is entitled, ~~to receive~~ whether or not actual damage or loss is proved to have been caused thereby to receive from the party who has broken the contract reasonable compensation not exceed in, the amount so named or is the case may be the penalty stipulated for

*Explanation* — A stipulation for increased interest from the date of default may be a stipulation by way of penalty |

*Exemption* — When any person enters into any bail-bond or guarantee or other instrument of the same nature or under the provisions of any law or under the orders of the [Central Government] or of any [Provincial Government], gives any bond for the performance of any public duty or act in which the public are interested, he shall be liable upon breach of the condition of any such instrument, to pay the whole sum mentioned therein

*Explanation* — A person, who enters into a contract with the Government does not necessarily thereby undertake any public duty to do in act in which the public are interested

*Illustrations.*

(a) A contracts with B to pay B Rs. 1,000 if he fails to pay B Rs. 500 on a given day. A fails to pay B Rs. 500 on that day. B is entitled to recover from A such compensation, not exceeding Rs. 1,000, as the Court considers reasonable.

(b) A contracts with B that, if A practises as a surgeon within Calcutta, he will pay B Rs. 5,000. A practises as a surgeon in Calcutta. B is entitled to such compensation, not exceeding Rs. 5,000, as the Court considers reasonable.

(c) A gives a recognizance binding him in a penalty of Rs. 500 to appear in Court on a certain day. He forfeits his recognizance. He is liable to pay the whole penalty.

(d) A gives B a bond for the repayment of Rs. 1,000 with interest at 12 per cent at the end of six months, with a stipulation that in case of default, interest shall be payable at the rate of 75 per cent from the date of default. This is a stipulation by way of penalty, and B is only entitled to recover from A such compensation as the Court considers reasonable.

(e) A, who owes money to B, a money-lender, undertakes to repay him by delivering to him 10 maunds of grain on a certain date, and stipulates that, in the event of his not delivering the stipulated amount by the stipulated date, he shall be liable to deliver 20 maunds. This is a stipulation by way of penalty, and B is only entitled to reasonable compensation in case of breach.

(f) A undertakes to repay B a sum of Rs. 1,000 by five equal monthly instalments with a stipulation that in default of payment of any instalment, the whole shall become due. This stipulation is not by way of penalty, and the contract may be enforced according to its terms.

(g) A borrows Rs. 1,000 from B and gives him a bond for Rs. 200 payable by five yearly instalments of Rs. 40, with a stipulation that, in default of payment of any instalment, the whole shall become due. This is a stipulation by way of penalty.

Party rightfully rescinding contract entitled to compensation

75. A person who rightfully rescinds a contract is entitled to compensation for any damage which he has sustained through the non-fulfilment of the contract.

*Illustration.*

A, a singer, contracts with B, the manager of a theatre, to sing at his theatre for two nights in every week during the next two months, and B engages to pay her 100 rupees for each night's performance. On the sixth night, A wilfully absents herself from the theatre, and B in consequence, rescinds the contract. B is entitled to claim compensation for the damage which he has sustained through the non-fulfilment of the contract

## CHAPTER VII.

### Of Indemnity and Guarantee.

124. A contract by which one party promises to save the other from loss caused to him by the "Contract of indemnity". In conduct of the promisor himself, or by the conduct of any other person, is called a "contract of indemnity".

*Illustration.*

A contracts to indemnify B against the consequences of any proceedings which C may take against B in respect of a certain sum of 200 rupees. This is a contract of indemnity.

125. The promisee in a contract of indemnity, acting with Rights of Indemni ty-holder when sued in the scope of his authority, is entitled to recover from the promisor—

- (1) all damages which he may be compelled to pay in any suit in respect of any matter to which the promise to indemnity applies :

- (2) all costs which he may be compelled to pay in any such suit if, in bringing or defending it, he did not contravene the orders of the promisor, and acted as it would have been prudent for him to act in the absence of any contract of indemnity, or if the promisor authorised him to bring or defend the suit ;
- (3) all sums which he may have paid under the terms of any compromise of any such suit, if the compromise was not contrary to the orders of the promisor, and was one which it would have been prudent for the promisee to make in the absence of any contract of indemnity, or if the promisor authorised him to compromise the suit.

126. A "contract of guarantee" is a contract to perform the promise, or discharge the liability, of a third person in case of his default. The person who gives the guarantee is called the "surety"; the person in respect of whose default the guarantee is given is called the "principal debtor", and the person to whom the guarantee is given is called the "creditor." A guarantee may be either oral or written.

127. Anything done, or any promise made, for the benefit of the principal debtor may be a sufficient consideration for giving the guarantee.

#### *Illustrations.*

(a) B requests A to sell and deliver to him goods on credit. A agrees to do so, provided C will guarantee the payment of the price of the goods. C promises to guarantee the payment in consideration of A's promise to deliver the goods. This is a sufficient consideration for C's promise.

(b) A sells and delivers goods to B. C afterwards requests A to forbear to sue B for the debt for a year and promises that

if he does so, C will pay for them in default of payment by B. A agrees to forbear as requested. This is a sufficient consideration for C's promise.

(c) A sells and delivers goods to B. C afterwards, without consideration, agrees to pay for them in default of B. The agreement is void.

128. The liability of the surety is co-extensive with that of Surety's liability. the principal debtor, unless it is otherwise provided by the contract.

*Illustration.*

A guarantees to B the payment of a bill of exchange by C, the acceptor. The bill is dishonoured by C. A is liable not only for the amount of the bill but also for any interest and charges which may have become due on it.

129. A guarantee which extends to a series of transaction is called a "continuing guarantee."

*Illustrations.*

(a) A, in consideration that B will employ C in collecting the rents of B's zamindari, promises B to be responsible, to the amount of 5,000 rupees, for the due collection and payment by C of those rents. This is a continuing guarantee.

(b) A guarantees payment to B, a tea-dealer, to the amount of £100, for any tea he may from time to time supply to C. B supplies C with tea to above the value of £100, and C pays B for it. Afterwards B supplies C with tea to the value of £200. C fails to pay. The guarantee given by A was a continuing guarantee, and he is accordingly liable to B to the extent of £100.

(c) A guarantees payment to B of the price of five sacks of flour to be delivered by B to C and to be paid for in a month. B delivers five sacks to C. C pays for them. Afterwards B delivers four sacks to C, which C does not pay for. The guarantee given by A was not a continuing guarantee, and accordingly he is not liable for the price of the sacks.

Revocation of continuing guarantee.

130. A continuing guarantee may at any time be revoked by the surety, as to future transactions, by notice to the creditor.

*Illustrations.*

(a) A, in consideration of B's discounting, at A's request, bills of exchange for C, guarantees to B, for twelve months, the due payment of all such bills to the extent of 5,000 rupees. B discounts bills for C to the extent of 2,000 rupees. Afterwards, at the end of three months, A revokes the guarantee. This revocation discharges A from all liability to B for any subsequent discount. But A is liable to B for the 2,000 rupees, on default of C.

(b) A guarantees to B, to the extent of 10,000 rupees, that C shall pay all the bills that B shall draw upon him. B draws upon C. C accepts the bill. A gives notice of revocation. C dishonours the bill at maturity. A is liable upon his guarantee.

Revocation of continuing guarantee by surety's death

131. The death of the surety operates, in the absence of any contract to the contrary, as a revocation of a continuing guarantee, so far as regards future transactions.

132. Where two persons contract with a third person to undertake a certain liability, and also contract with each other that one of them shall be liable only on the default of the other, the third person not being a party to such contract, the liability of each of such two persons to the third person under the first contract is not affected by the existence of the second contract, although such third person may have been aware of its existence.

Liability of two persons, primarily liable, not affected by arrangement between them that one shall be surety on other's default

133. Where two persons contract with a third person to undertake a certain liability, and also contract with each other that one of them shall be liable only on the default of the other, the third person not being a party to such contract, the liability of each of such two persons to the third person under the first contract is not affected by the existence of the second contract, although such third person may have been aware of its existence.

*Illustration.*

A and B make a joint and several promissory note to C. A makes it, in fact, as surety for B, and C knows this at the time

when the note is made. The fact that A, to the knowledge of C, made the note as surety for B, is no answer to a suit by C against A upon the note.

133. Any variance, made without  
Discharge of surety's consent, in the terms of the contract between the principal debtor and creditor, discharges the surety as to transactions subsequent to the variance

by variance in terms of contract.

*Illustrations.*

(a) A becomes surety to C for B's conduct as a manager of C's band. Afterwards, B and C contract, without A's knowledge, that B's salary shall be raised, and that he shall become liable for one-fourth of the losses on overdrafts. B allows a customer to overdraw and the bank loses a sum of money. A is discharged from the suretyship by the variance made without his knowledge and is not liable to make good this loss.

(b) A guarantees C against the misconduct of B in an office to which B is appointed by C, and of which the duties are defined by an Act of the Legislature. By a subsequent Act, the nature of the office is materially altered. Afterwards, B misbehaves himself. A is discharged by the change from future liability under his guarantee, though the misconduct of A is in respect of a duty not affected by the later Act.

(c) C agrees to appoint B as his clerk to sell goods at yearly salary, upon A's becoming surety to C for B's duly accounting for moneys received by him as such clerk. Afterwards, without A's knowledge or consent, C and B agree that B should be paid by a commission on the goods sold by him and not by a fixed salary. A is not liable for subsequent misconduct of B.

(d) A gives to C a continuing guarantee to the extent of 3,000 rupees for any oil supplied by C to B on credit. Afterwards, B becomes embarrassed, and, without the knowledge of A, B and C contract that C shall continue to supply B with oil for ready money, and that the payments shall be applied to the then existing

ing debts between B and C. A is not liable on his guarantee for any goods supplied after this new arrangement.

(e) C contracts to lend B 5,000 rupees on the 1st March. A guarantees repayment. C pays the 5,000 rupees to B on the 1st January. A is discharged from his liability, as the contract has been varied in as much as C might sue B for the money before the 1st of March.

**144. The surety is discharged by any contract between the creditor and the principal debtor, by which the principal debtor is released, or by any act or omission of the creditor, the legal consequence of which is the discharge of the principal debtor.**

Discharge of surety  
by release or discharge  
of principal debtor

#### *Illustrations:*

(a) A gives a guarantee to C for goods to be supplied by C to B. C supplies goods to B, and afterwards B becomes embarrassed and contracts with his creditors (including C) to assign to them his property in consideration of their releasing him from their demands. Here B is released from his debt by the contract with C, and A is discharged from his suretyship.

(b) A contracts with C to grow a crop of indigo on A's land and to deliver it to B at a fixed rate, and C guarantees A's performance of this contract. It diverts a stream of water which is necessary for irrigation of A's land and thereby prevents him from raising the indigo. C is no longer liable on his guarantee.

(c) A contracts with B for a fixed price to build a house for B within a stipulated time, B supplying the necessary timber. C guarantees A's performance of the contract. B omits to supply the timber. C is discharged from his suretyship.

Discharge of surety  
when creditor com-  
pounds with, gives  
time to, or agrees not  
to sue, principal  
debtor.

**135. A contract between the creditor and the principal debtor, by which the creditor makes a composition with, or promises to give time to, or not to sue, the principal debtor, discharges the surety, unless the surety assents to such contract.**

Surety not discharged when agreement made with third persons to give time to principal debtor

136 Where a contract to give time to the principal debtor is made by the creditor with a third person, and not with the principal debtor, the surety is not discharged

*Illustration.*

C, the holder of an overdue bill of exchange drawn by A as surety for B, and accepted by B, contracts with M to give time to B. A is not discharged

137 Merit forbearance on the part of the creditor to sue the principal debtor or to enforce any other remedy against him does not, in the absence of any provision in the guarantee to the contrary, discharge the surety

*Illustration*

B owes to C a debt guaranteed by A. The debt becomes payable. C does not sue B for 1 year after the debt has become payable. A is not discharged from his suretymship

138 Where there are co-sureties a release by the creditor of one of them does not discharge the others, neither does it free the surety so released from his responsibility to the other sureties

139 If the creditor does any act which is inconsistent with the rights of the surety or omits to do any act which his duty to the surety requires him to do, and the eventual remedy of the surety himself against the principal debtor is thereby impaired the surety is discharged

Discharge of surety by creditor's act or omission impairing surety's eventual remedy

*Illustration.*

(a) B contracts to build a ship for C for a given sum, to be paid by instalments as the work reaches certain stages. A becomes surety to C for B's due performance of the contract

C, without the knowledge of A, prepays to B the last two instalments. A is discharged by this prepayment.

(b) C lends money to B on the security of a joint and several promissory note made in C's favour by B, and by A as surety for B, together with a bill of sale of B's furniture, which gives power to C to sell the furniture, and apply the proceeds in discharge of the note. Subsequently, C sells the furniture, but, owing to his misconduct and wilful negligence, only a small price is realized. A is discharged from liability on the note.

(c) A puts M as apprentice to B, and gives a guarantee to B, for M's fidelity. B promises on his part that he will, at least once a month, see M make up the cash. B omits to see this done as promised, and M embezzles. A is not liable to B on his guarantee.

140. Where a guaranteed debt has become due, or default of the principal debtor to perform a guaranteed duty has taken place, the surety, upon payment or performance of all that he is liable for, is invested with all the rights which the creditor had against the principal debtor.

141. A surety is entitled to the benefit of every security which the creditor has against the principal debtor at the time when the contract of suretyship is entered into, whether the surety knows of the existence of such security or not; and, if the creditor loses or, without the consent of the surety, parts with such security, the surety is discharged to the extent of the value of the security.

#### *Illustrations.*

(a) C advances to B, his tenant, 2,000 rupees on the guarantee of A. C has also a further security for the 2,000 rupees by a mortgage of B's furniture. C cancels the mortgage. B becomes insolvent, and C sues A on his guarantee. A is discharged from liability to the amount of the value of the furniture.

(b) C, a creditor, whose advance to B is secured by a decree receives also a guarantee for that advance from A. C afterwards takes B's goods in execution under the decree, and then, without the knowledge of A, withdraws the execution. A is discharged.

(c) A, as surety for B, makes a bond jointly with B to C, to secure a loan from C to B. Afterwards, C obtains from B a further security for the same debt. Subsequently, C gives up the further security. A is not discharged.

**Guarantee obtained by misrepresentation invalid**

142. Any guarantee which has been obtained by means of misrepresentation made by the creditor, or with his knowledge and assent, concerning a material part of the transaction, is invalid.

**Guarantee obtained by concealment invalid**

143. Any guarantee which the creditor has obtained by means of keeping silence as to material circumstances is invalid

#### *Illustration.*

(a) A engages B as clerk to collect money for him. B fails to account for some of his receipts, and A in consequence calls upon him to furnish security for his duly accounting. C gives his guarantee for B's duly accounting. A does not acquaint C with B's previous conduct. B afterwards makes default. The guarantee is invalid.

(b) A guarantees to C payment for iron to be supplied by him to B to the amount of 2,000 tons. B and C have privately agreed that B should pay five rupees per ton beyond the market price, such excess to be applied in liquidation of an old debt. This agreement is concealed from A. A is not liable as a surety.

**Guarantee on condition that creditor shall not act on it until co-surety joins**

144. Where a person gives a guarantee upon a contract that the creditor shall not act upon it until another person has joined in it as co-surety, the guarantee is not valid if that other person does not join

**145.** In every contract of guarantee there is an implied promise by the principal debtor to indemnify the surety; and the surety is entitled to recover from the principal debtor whatever sum he has rightfully paid under the guarantee, but no sums which he has paid wrongfully

Implied promise to  
indemnify surety

#### *Illustrations.*

(a) B is indebted to C, and A is surety for the debt. C demands payment from A, and on his refusal sues him for the amount. A defends the suit, having reasonable grounds for doing so but is compelled to pay the amount of the debt with costs. He can recover from B the amount paid by him for costs, as well as the principal debt.

(b) C lends B a sum of money, and A, at the request of B, accepts a bill of exchange drawn by B upon A to secure the amount. C the holder of the bill, demands payment of it from A, and, on A's refusal to pay, sues him upon the bill. A, not having reasonable grounds for so doing, defends the suit, and has to pay the amount of the bill and costs. He can recover from B the amount of the bill, but not the sum paid for costs as there was no real ground for defending the action.

(c) A guarantees to C, to the extent of 2,000 rupees, payment for rice to be supplied by C to B. C supplies to B rice to a less amount than 2,000 rupees, but obtains from A payment of the sum of 2,000 rupees in respect of the rice supplied. A cannot recover from B more than the price of the rice actually supplied.

**146** Where two or more persons are co-sureties for the same debt or duty, either jointly or severally, and whether under the same or different contracts, and whether

Co-sureties liable to  
contribute equally

with or without the knowledge of each other, the co-sureties in the absence of any contract to the contrary, are liable as between themselves, to pay each an equal shares of the whole debt, or of that part of it which remains unpaid by the principal debtor.

~~(a) A, B and C are sureties to D for the sum of 3,000 rupees, conditioned for D's duly accounting to payment. A, B and C are liable to pay 1,000 rupees each.~~

~~(b) A, B and C are sureties to D for the sum of 1,000 rupees, conditioned for D's duly accounting to payment. There is a contract between A, B and C that A is liable to the extent of one-quarter, B to the extent of one-quarter, and C to the extent of one half. D makes default to payment. As between the sureties, A is liable to pay 250 rupees, B 250 rupees, and C 500 rupees.~~

**Liability of co-sureties bound in different sums.** Different sums are liable to pay equally as far as the limits of their respective obligations permit.

#### *Illustrations.*

(a) A, B and C, as sureties for D, enter into three several bonds, each in a different penalty, namely, A in the penalty of 10,000 rupees, B in that of 20,000 rupees, C in that of 40,000 rupees, conditioned for D's duly accounting to E. D makes default to the extent of 30,000 rupees. A, B and C are each liable to pay 10,000 rupees.

(b) A, B and C, as sureties for D, enter into three several bonds, each in a different penalty, namely, A in the penalty of 10,000 rupees, B in that of 20,000 rupees, C in that of 40,000 rupees, conditioned for D's duly accounting to E. D makes default to the extent of 40,000 rupees. A is liable to pay 10,000 rupees, and B and C 15,000 rupees.

(c) A, B and C, as sureties for D, enter into three several bonds, each in a different penalty, namely, A in the penalty of 10,000 rupees, B in that of 20,000 rupees, C in that of 40,000 rupees, conditioned for D's duly accounting to E. D makes default to the extent of 70,000 rupees. A, B and C have to pay each the full penalty of his bond.

## CHAPTER IX

### Of Bailment

148. A "bailment" is the delivery of goods by one person to another for some purpose, upon a contract that they shall when the purpose is accomplished, be returned or otherwise disposed of according to the directions of the person delivering them. The person delivering the goods is called the "bailor". The person to whom they are delivered is called the "bailee".  
"Bailment" "bailor" and "bailee" defined

**Explanation**—If a person already in possession of the goods of another contracts to hold them as a bailee, he thereby becomes the bailee, and the owner becomes the bailor, of such goods although they may not have been delivered by way of bailment.

149. The delivery to the bailee may be made by doing anything which has the effect of putting the goods in the possession of the intended bailee or of any person authorized to hold them on his behalf.  
**Delivery to bailee how made**

150. The bailor is bound to disclose to the bailee faults in the goods bailed, of which the bailor is aware, and which materially interfere with the use of them or expose the bailee to extraordinary risks, and, if he does not make such disclosure, he is responsible for damage arising to the bailee directly from such faults.  
**Bailor's duty to disclose faults in goods bailed**

If the goods are bailed for hire, the bailor is responsible for such damage, whether he was or was not aware of the existence of such faults in the goods bailed.

### *Illustration*

(a) A lends a horse which he knows to be vicious to B. He does not disclose the fact that the horse is vicious. The horse

**150. Bailee's carriage of B.** The carriage of goods, though not agent of A, and A is injured. B is responsible to A for the injury.

151. In all cases of bailment the bailee is bound to take as

*Care to be taken by  
bailee.*  
much care of the goods bailed to him as a man of ordinary prudence would, under similar circumstances, take of his own goods of the same bulk, quality and value as the goods bailed.

152. The bailee, in the absence of any special contract, is

*Bailee when not  
liable for loss, etc, of  
thing bailed.*  
not responsible for the loss, destruction or deterioration of the thing bailed, if he has taken the amount of care of it described in section 151.

153 A contract of bailment is voidable at the option of the bailor, if the bailee does any act with regard to the goods bailed, inconsistent with the conditions of the bailment.

#### *Illustration*

A lets to B, for hire, a horse for his own riding. B drives the horse in his carriage. This is, at the option of A, a termination of the bailment.

154. If the bailee makes any use of the goods bailed, which

*Liability of bailee  
making unauthorized  
use of goods bailed.*  
is not according to the conditions of the bailment, he is liable to make compensation to the bailor for any damage arising to the goods from or during such use of them.

#### *Illustrations*

(a) A lends a horse to B for his own riding only. B allows C, a member of his family, to ride the horse. C rides with care but the horse, accidentally falls and is injured. B is liable to make compensation to A for the injury done to the horse.

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(d) A hires a horse in Calcutta from B expressly to go to Benares. A rides with due care, but marches to Cuttack instead. The horse accidentally falls and is injured. A is liable to make compensation to B for the injury to the horse.

155. If the bailee, with the consent of the bailor, mixes the

Effect of mixture  
with bailor's consent  
of his goods with  
bailee's  
goods  
the goods of the bailor with his own goods, the bailor and bailee shall have an interest in proportion to their respective shares, in the mixture thus produced

156. If the bailee, without the consent of the bailor, mixes the goods of the bailor with his own goods,

Effect of mixture  
without bailor's con-  
sent when the goods  
can be separated  
and the goods can be separated or divided,  
the property in the goods remains in the parties respectively, but the bailee is bound to bear the expense of separation or division, and any damage arising from the mixture

*Illustration*

A hauls 100 bales of cotton marked with a particular mark to B. B, without A's consent, mixes the 100 bales with others bales of his own bearing a different mark. A is entitled to have his 100 bales returned, and B is bound to bear all the expenses incurred in the separation of the bales, and any other incidental damage.

157. If the bailee, without the consent of the bailor, mixes the goods of the bailor with his own goods,

Effect of mixture  
without bailor's con-  
sent when the goods  
cannot be separated  
in such a manner that it is impossible to separate the goods haled from the other goods and deliver them back, the bailor is entitled to be compensated by the bailee for the loss of the goods

*Illustration*

A hauls a barrel of Cape flour worth Rs 45 to B. B, without A's consent, mixes the flour with country flour of his own, worth only Rs 25 a barrel, B must compensate A for the loss of his flour.

158. Where, by the conditions of the bailment, the goods are to be kept or to be carried, or to have work done upon them

*Repayment by bailor of necessary expenses.* by the bailee for the bailor and the bailee is to receive no remuneration, the bailor shall repay to the bailee the necessary expenses incurred by him for the purpose of the bailment.

159. The lender of a thing for use may at any time require its return, if the loan was gratuitous even though he lent it for a

*Restoration of goods lent gratuitously.* specified time or purpose. But if, on the faith of such loan made for a specified time or purpose, the borrower has acted in such a manner that the return of the thing lent before the time agreed upon would cause him loss exceeding the benefit actually derived by him from the loan, the lender must, if he compels the return, indemnify the borrower for the amount in which the loss so occasioned exceeds the benefit so derived.

160. It is the duty of the bailee to return, or deliver according to the bailor's directions, the goods bailed, without demand, as soon as the

*Return of goods bailed on expiration of time or accomplishment of purpose.* time for which they were bailed has expired, or the purpose for which they were bailed has been accomplished.

161. If by the default of the bailee, the goods are not returned, delivered or tendered at the proper time, he is responsible to the bailor for any loss, destruction or deterioration of the goods from that time.

*Bailee's responsibility when goods are not duly returned.*

Termination of gratuitous bailment by death

162. A gratuitous bailment is terminated by the death either of the bailor or of the bailee.

163. In the absence of any contract to the contrary, the bailee is bound to deliver to the bailor, or according to his directions, any increase or profit which may have accrued from the goods bailed.

*Bailor entitled to increase or profit from goods bailed.*

*Illustration*

A leaves a cow in the custody of B to be taken care of. The cow has a calf. B is bound to deliver the calf as well as the cow to A.

164 The bailor is responsible to the bailee for any loss which the bailee may sustain by reason that the bailor was not entitled to make the bailment, or to receive back the goods or to give directions respecting them.

Bailor's responsibility to bailee

165 If several joint owners of goods bail them, the bailee may deliver them back to, or according to the directions of, one joint owner without the consent of all, in the absence of any agreement to the contrary.

Bailment by several joint owners

166 If the bailor has no title to the goods, and the bailee, in good faith, delivers them back to, or according to directions of the bailor, the bailee is not responsible to the owner in respect of such delivery.

Bailee not responsible on re-delivery to bailor without title

Right of third person claiming goods bailed

167 If a person, other than bailor, claims goods bailed, he may apply to the court to stop the delivery of the goods to the bailor, and to decide the title to the goods.

168 The finder of goods has no right to use the owner for compensation for trouble and expense voluntarily incurred by him to preserve the goods and to find out the owner: but he may retain the goods against the owner until he receives such compensation: and, where the owner has offered a special reward for the return of goods lost, the finder may sue for such reward, and may retain the goods until he receives it.

Right of finder of goods may sue for specific reward offered

169. When a thing which is commonly the subject of sale is lost, if the owner cannot with reasonable diligence be found, or if he refuses, upon demand, to pay the lawful charges of the sale may sell it.

When finder of thing commonly on demand, to pay the lawful charges of the sale may sell it. finder, the finder may sell it—

(1) when the thing is in danger of perishing or of losing the greater part of its value, or,

(2) when the lawful charges of the finder in respect of the thing found, amount to two-thirds of its value.

170. Where the bailee has, in accordance with the purpose of the bailment, rendered any service involving the exercise of

Bailee's particular labour or skill in respect of the goods bailed, he has, in the absence of a contract to the contrary, a right to retain such goods until he receives due remuneration for the services he has rendered in respect of them.

#### *Illustrations*

(a) A delivers a rough diamond to B, a jeweller, to be cut and polished, which is accordingly done. B is entitled to retain the stone till he is paid for the services he has rendered.

(b) A gives cloth to B, a tailor, to make into a coat. B promises A to deliver the coat as soon as it is finished, and to give a three month's credit for the price. B is not entitled to retain the coat until he is paid.

171. Bankers, factors, wharfingers, attorneys of a High Court and policy-brokers may, in the absence of a contract to the contrary, retain, as a security for a general

General lien of bankers, factors, wharfingers, attorney, and policy-brokers. balance of account, any goods bailed to them; but no other persons have a right to retain as a security for such balance, goods bailed to them, unless there is an express contract to that effect.

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*Bailments of Pledges*

172. The bailment of goods as security for payment of a debt or performance of a promise is called 'pledge'. 'pawnor' & 'pawnee' defined  
The bailor is in this case called the 'pawnor'. The bailee is called the 'pawnee'.

173. The pawnee may retain the goods pledged, not only for payment of the debt or the performance of the promise, but for the interest of the debt, and all necessary expenses incurred by him in respect of the possession or for the preservation of the goods pledged.

174. The pawnee shall not, in the absence of a contract to that effect, retain the goods pledged for and debt or promise other than the debt or promise for which they are pledged; but such contract, in the absence of anything to the contrary, shall be presumed in regard to subsequent advances made by the pawnee.

Pawnee's right not to retain for debt or promise other than that for which goods pledged. Presumption in case of subsequent advances.  
175. The pawnee is entitled to receive from the pawnor extraordinary expenses incurred by him for the preservation of the goods pledged.

176. If the pawnor makes default in payment of the debt, or performance, at the stipulated time of the promise, in respect where pawnor makes default of which the goods were pledged, the pawnee may bring a suit against the pawnor upon the debt or promise, and retain the goods pledged as collateral security; or he may sell the thing pledged on giving the pawnor reasonable notice of the sale.

If the proceeds of such sale are less than the amount due in respect of the debt or promise, the pawnor is still liable to pay the balance. If the proceeds of the sale are greater than the

amount so due, the pawnee shall pay over the surplus to the pawnor.

177. If a time is stipulated for the payment of the debt, or performance of the promise, for which the pledge is made, and the pawnor makes default in payment of the debt or performance of the promise at the stipulated time, he may redeem the goods pledged at any subsequent time before the actual sale of them ; but he must, in that case, pay, in addition any expenses which have arisen from his default.

178. Where a mercantile agent is, with the consent of the owner, in possession of goods or the documents of title to goods, any pledge made by him, when acting in the ordinary course of business of a mercantile agent, shall be as valid as if he were expressly authorised by the owner of the goods to make the same ; provided that the pawnee acts in good faith and has not at the time of the pledge notice that the pawnor has not authority to pledge.

*Explanation.*—In this section, the expressions 'mercantile agent', and 'documents of title' shall have the meanings assigned to them in the Indian Sale of Goods Act, 1930.

178A. When the pawnor has obtained possession of the goods pledged by him under a contract voidable under section 19 or section 19A, but the contract has not been rescinded at the time of the pledge, the pawnee acquires a good title to the goods, provided, he acts in good faith and without notice of the pawnor's defect of title.

Pledge where pawnor has only a limited interest  
179. Where a person pledges goods in which he has only a limited interest, the pledge is valid to the extent of that interest.

*Suits by Bailees or Bailors against Wrong-doers.*

180. If a third person wrongfully deprives the bailee of the use or possession of the goods bailed, or does them any injury,

*Suit by bailor or bailee against wrong-doer.*  
the bailee is entitled to use such remedies as the owner might have used in the like case if no bailment had been made; and either the bailor or the bailee may bring a suit against a third person for such deprivation or injury.

*Appointment of relief or compensation obtained by such suits.*

181. Whatever is obtained by way of relief or compensation in any such suit shall, as between the bailor and the bailee, be dealt with according to their respective interests.

## CHAPTER X

## Agency

*Appointment and Authority of Agents.*

182. An "agent" is a person employed to do any act for another or to represent another in dealings with third persons. The person for whom such act is done, or who is so represented, is called the "principal".

*Who may employ agent.*

183. Any person who is of the age of majority according to the law to which he is subject, and who is of sound mind, may employ an agent.

*Who may be an agent.*

184. As between the principal and third persons any person may become an agent, but no person who is not of the age of majority and of sound mind can become an agent, so as to be responsible to his principal according to the provisions in that behalf herein contained.

Consideration not necessary.

Agent's authority may be expressed or implied.

187. An authority is said to be expressed when it is given by words spoken or written. An authority is said to be implied when

Definitions of express implied authority. it is to be inferred from the circumstances of the case ; and things spoken or written, or the ordinary course of dealing, may be accounted circumstances of the case.

185. No consideration is necessary to create an agency.

186. The authority of an agent may be expressed or implied.

*Illustration*

A owns a shop in Serampur, living himself in Calcutta, and visiting the shop occasionally. The shop is managed by B, and he is in the habit of ordering goods from C in the name of A for the purpose of the shop, and of paying for them out of A's funds with A's knowledge. B has an implied authority from A to order goods from C in the name of A for the purposes of the shop.

188. An agent having an authority to do an act has authority to do every lawful thing which is necessary in order to do such act.

An agent having an authority to carry on a business has authority to do every lawful thing necessary for the purpose, or usually done in the course of conducting such business.

*Illustrations*

(a) A is employed by B, residing in London, to recover at Bombay a debt due to B. A may adopt any legal process necessary for the purpose of recovering the debt and may give a valid discharge for the same.

(b) A constitutes B his agent to carry on his business of a shipbuilder. B may purchase timber and other materials, and hire workmen, for the purposes of carrying on the business.

**189.** An agent has authority, in an emergency, to do all such acts for the purpose of protecting his principal from loss as would be done by a person of ordinary prudence, in his own case, under similar circumstances.

Agent's authority in an emergency.

### *Illustrations*

(a) An agent for sale may have goods repaired if it be necessary.

(b) A consigns provisions to B at Calcutta, with directions to send them immediately to C at Cuttack. B may sell the provisions at Calcutta, if they will not bear the journey to Cuttack without spoiling.

### *Sub-Agent.*

**190.** An agent cannot lawfully employ another to perform acts which he has expressly or impliedly undertaken to perform personally, unless by the ordinary custom of trade a sub-agent may, or from the nature of the agency, a sub-agent must be employed.

When agent cannot delegate.

**191.** A "sub-agent" is a person employed by, and acting under the control of, the original agent in the business of the agency.

Sub-agent" defined

**192.** Where a sub-agent is properly appointed the principal is, so far as regards third persons, represented by the sub-agent, and is bound by and responsible for his acts as if he were an agent originally appointed by the principal.

Representation of principal by sub agent properly appointed

The agent is responsible to the principal for the acts of the sub-agent :

Agent's responsibility for sub-agents

The sub-agent is responsible for his acts to the agents, but not to the principal, except in case of fraud or wilful wrong.

Sub-agent's responsibility

**193.** Where an agent, without having authority to do so, has

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appointed a person to act as a sub-agent, the agent stands towards such person in the relation of a principal to an agent, and is responsible for his acts both to the principal and to third persons ; the principal is not represented by or responsible for acts of the person so employed, nor is that person responsible to the principal.

**194.** Where an agent, holding an express or implied authority to name another person to act for the principal in the business of the agency, has named another person accordingly, such person is not a sub-agent but an agent of the principal for such part of the business of the agency as is entrusted to him.

#### *Illustrations.*

(a) A directs B, his solicitor, to sell his estate by auction, and to employ an auctioneer for the purpose. B names C, an auctioneer, to conduct the sale. C is not a sub-agent, but is A's agent for the conduct of the sale.

(b) A authorizes B, a merchant in Calcutta, to recover the moneys due to A from C & Co., B instructs D, a solicitor, to take legal proceedings against C & Co., for the recovery of the money. D is not a sub-agent but is solicitor for A.

**195.** In selecting such agent for his principal, an agent is bound to exercise the same amount of discretion as a man of ordinary prudence would exercise in his own case ; and if he does this he is not responsible to the principal for the acts or negligence of the agent so selected.

#### *Illustrations.*

(a) A instructs B, a merchant, to buy a ship for him. B employs a ship surveyor of good reputation to choose a ship for A. The surveyor makes the choice negligently and the ship turns

out to be unseaworthy and is lost. B is not, but the surveyor is responsible to A.

(b) A consigns goods to B, a merchant, for sale. B, in due course, employs an auctioneer in good credit to sell the goods of A, and allows the auctioneer to receive the proceeds of the sale. The auctioneer afterwards becomes insolvent without having accounted for the proceeds. B is not responsible to A for the proceeds.

### *Ratification.*

196. Where acts are done by one person on behalf of another, but without his knowledge or authority, he may elect to ratify or to disown such acts.

Right of person is to acts done for him without his authority  
Effect of ratification

If he ratifies them, the same effects will follow as if they had been performed by his authority

197. Ratification may be expressed or implied in the conduct of the person on whose behalf the acts are done.

### *Illustrations.*

(a) A, without authority, buys goods for B. Afterwards B sells them to C on his own account; B's conduct implies a ratification of the purchase made for him by A.

(b) A, without B's authority, lends B's money to C. Afterwards B accepts interest on the money from C. B's conduct implies a ratification of the loan.

Knowledge requisite for valid ratification

Effect of ratifying unauthorized act forming part of a transaction.  
formed a part.

198. No valid ratification can be made by a person whose knowledge of the facts of the case is materially defective.

199. A person ratifying any unauthorized act done on his behalf ratifies the whole of the transaction of which such act

**200. An act done by one person on behalf of another, without such other person's authority, which, if done with authority, would have the effect of subjecting a third person to damages, or of terminating any right or interest of a third person, cannot, by ratification, be made to have such effect.**

**Ratification of unauthorized act cannot injure third person.**

done with authority, would have the effect of subjecting a third person to damages, or of terminating any right or interest of a third person, cannot, by ratification, be made to have such effect.

#### *Illustrations.*

(a) A, not being authorized thereto by B, demands on behalf of B, the delivery of a chattel, the property of B, from C, who is in possession of it. This demand cannot be ratified by B, so as to make C liable for damages for his refusal to deliver.

(b) A holds a lease from B, terminable on three months' notice. C, an unauthorized person, gives notice of termination to A. The notice cannot be ratified by B, so as to be binding on A.

#### *Revocation of Authority.*

**201. An agency is terminated by the principal revoking his authority ; or by the agent renouncing the business of the agency**

**Termination of agency.** or by the business of the agency being completed; or by either the principal or agent dying or becoming of unsound mind; or by the principal being adjudicated an insolvent under the provisions of any Act for the time being in force for the relief of insolvent debtors.

**Termination of agency where agent has an interest in subject-matter**

**202. Where the agent has himself an interest in the property which forms the subject-matter of the agency, the agency cannot, in the absence of an express contract, be terminated to the prejudice of such interest.**

#### *Illustrations.*

(a) A gives authority to B to sell A's land, and to pay himself, out of the proceeds, the debts due to him from A. A cannot revoke this authority, nor can it be terminated by his insanity or death.

(b) A consigns 1,000 bales of cotton to B, who has made advances to him on such cotton, and desires B to sell the cotton, and to repay himself out of the price, the amount of his own

advances. A cannot revoke this authority, nor is it terminated by his insanity or death.

**203.** The principal may, save as is otherwise proved by the When principal may revoke agent's authority. last preceding section, revoke the authority given to his agent at any time before the authority has been exercised so as to bind the principal.

**204.** The principal cannot revoke the authority given to his agent after the authority has been partly exercised so far as regards such acts and obligations as arise from acts already done in the agency.  
Revocation where authority has been partly exercised.

#### *Illustrations.*

(a) A authorizes B to buy 1,000 bales of cotton on account of A, and to pay for it out of A's money remaining in B's hands. B buys 1,000 bales of cotton in his own name, so as to make himself personally liable for the price. A cannot revoke B's authority so far as regards payment for the cotton.

(b) A authorizes B to buy 1,000 bales of cotton on account of A, and to pay for it out of A's moneys remaining in B's hands. B buys 1,000 bales of cotton in A's name and so as not to render himself personally liable for the price. A can revoke B's authority to pay for the cotton.

**205.** Where there is an express or implied contract that the compensation for revocation by principal or renunciation by agent. agency should be continued for any period of time, the principal must make compensation to the agent, or the agent to the principal as the case may be, for any previous revocation or renunciation of the agency without sufficient cause.

**206.** Reasonable notice must be given of such revocation or renunciation : otherwise the damage thereby resulting to the principal or the agent, as the case may be, must be made good to the one by the other.  
Notice of revocation or renunciation.

**Revocation and renunciation may be expressed or implied.**

**207.** Revocation and renunciation may be expressed or may be implied in the conduct of the principal or agent respectively.

*Illustrations.*

A empowers B to let A's house. Afterwards A lets it himself. This is an implied revocation of B's authority.

**208.** The termination of the authority of an agent does not, so far as regards the agent, take effect before it becomes known to him, or so far as regards third persons, before it becomes known to them.

*Illustrations.*

(a) A directs B to sell goods for him, and agrees to give B five per cent. commission on the price fetched by the goods. A afterwards, by letter, revokes B's authority. B after the letter is sent, but before he receives it, sells the goods for 100 rupees. The sale is binding on A, and B is entitled to five rupees as his commission.

(b) A, at Madras, by letter directs B to sell for him some cotton lying in a warehouse in Bombay, and afterwards by letter, revokes his authority to sell, and directs B to send the cotton to Madras. B, after receiving the second letter, enters into a contract with C, who knows of the first letter, but not of the second, for the sale to him of the cotton. C pays B the money, with which B absconds. C's payment is good as against A.

(c) A directs B, his agent, to pay certain money to C. A dies, and D takes out probate to his will. B, after A's death, but before hearing of it, pays the money to C. The payment is good as against D, the executor.

**209.** When an agency is terminated by the principal dying or becoming of unsound mind, the agent is bound to take, on behalf of the representatives of his late principal, all reasonable steps for the protection and preservation of the interests entrusted to him.

**Agent's duty on termination of agency by principal's death or insanity.**

**210. The termination of the authority of an agent causes the termination (subject to the rules herein contained regarding the termination of an agent's authority) of the authority of all sub-agents appointed by him.**

*Agent's Duty to Principal.*

**211. An agent is bound to conduct the business of his principal according to the directions given by the principal, or, in the absence of any such direction, according**

**Agent's duty in conducting principal's business** to the custom which prevails in doing business of the same kind at the place where the agent conducts such business.

When the agent acts otherwise, if any loss be sustained, he must make it good to his principal, and, if any profit accrues, he must account for it.

*Illustrations.*

(a) A, an agent engaged in carrying on for B a business, in which it is the custom to invest from time to time, at interest the moneys which may be in hand, omits to make such investment. A must make good to B the interest usually obtained by such investment.

(b) B, a broker, in whose business it is not the custom to sell on credit, sells goods of A on credit to C, whose credit at the time was very high. C, before payment, becomes insolvent. B must make good the loss to A.

**212. An agent is bound to conduct the business of the agency with as much skill as is generally possessed by persons engaged in similar business, unless the principal has notice of his want of skill. The agent is always bound to act with reasonable diligence, and to use such skill as he possesses; and to make compensation to his principal in respect of the direct consequences of his own neglect, want of skill or misconduct, but not in respect of loss or damage which are indirectly or remotely caused by such neglect, want of skill or misconduct.**

*Illustrations.*

(a) A, a merchant in Calcutta, has an agent, B, in London to whom a sum of money is paid on A's account, with orders to remit. B retains the money, for a considerable time. A, in consequence of not receiving the money, becomes insolvent. B is liable for the money and interest from the day on which it ought to have been paid, according to the usual rate, and for any further direct loss—as e.g., by variation of rate of exchange—but not further.

(b) A, an agent for the sale of goods, having authority to sell on credit, sells to B on credit without making proper and usual enquiries as to the solvency of B. B, at the time of such sale, is insolvent. A must make compensation to his principal in respect of any loss thereby sustained.

(c) A, an insurance-broker, employed by B to effect an insurance on a ship, omits to see that the usual clauses are inserted in the policy. The ship is afterwards lost. In consequence of the omission of the clauses nothing can be recovered from the underwriters. A is bound to make good the loss to B.

(d) A, a merchant in England directs B, his agent at Bombay who accepts the agency, to send him 100 bales of cotton by a certain ship. B, having it in his power to send the cotton, omits to do so. The ship arrives safely in England. Soon after her arrival the price of cotton rises. B is bound to make good to A the profit which he might have made by the 100 bales of cotton at the time the ship arrived; but not any profit he might have made by the subsequent rise.

Agent's accounts.

213. An agent is bound to render proper accounts to his principal on demand.

Agent's duty to communicate with principal.

214. It is the duty of an agent, in cases of difficulty, to use all reasonable diligence in communicating with his principal, and in seeking to obtain his instructions.

215. If an agent deals on his own account in the business of the agency without first obtaining the consent of his principal

Right of principal when agent deals, on his own account, in business of agency without principal's consent, and acquainting him with all material circumstances which have come to his own knowledge on the subject, the principal may repudiate the transaction, if the case shows either that any material fact has been dishonestly concealed from him by the agent, or that the dealings, of the agent have been disadvantageous to him.

#### *Illustrations.*

(a) A directs B to sell A's estate. B buys the estate for himself in the name of C. A, on discovering that B has bought the estate for himself, may repudiate the sale, if he can show that B has dishonestly concealed any material fact, or that the sale has been disadvantageous to him.

(b) A directs B to sell A's estate. B, on looking over the estate before selling it, finds a mine on the estate which is unknown to A. B informs A that he wishes to buy the estate for himself, but conceals the discovery of the mine. A allows B to buy, in ignorance of the existence of the mine. A on discovering that B knew of the mine at the time he bought the estate, may either repudiate or adopt the sale at his option.

216. If an agent, without the knowledge of his principal, Principal's right to benefit gained by agent dealing on his own account in business of agency. deals in the business of the agency on his own account instead of an account of his principal, the principal is entitled to claim from the agent any benefit which may have resulted to him from the transaction.

#### *Illustration.*

A directs B, his agent, to buy a certain house for him. B tells A it cannot be bought, and buys the house for himself. A may on discovering that B has bought the house, compel him to sell it to A at the price he gave for it.

**217.** An agent may retain, out of any sums received on account of the principal in the business of the agency, all moneys due to himself in respect of advances made or expenses properly incurred by him in conducting such business, and also such remuneration as

**Agent's right of re-tainer out of sums received on principal's account.**

may be payable to him for acting as agent.

**Agent's duty to pay sums received for principal.**

**218.** Subject to such deductions, the agent is bound to pay to his principal all sums received on his account.

**219.** In the absence of any special contract, payment for the performance of any act is not due to the agent until the completion of such act ; but an agent may detain moneys received by him on account of goods sold, although the whole of the goods

**When agent's remuneration becomes due.**  
consigned to him for sale may not have been sold, or although the sale may not be actually complete.

**220.** An agent who is guilty of misconduct in the business of the agency is not entitled to any remuneration in respect of that part of the business which he has misconducted.

#### *Illustrations.*

(a) A employs B to recover 1,00,000 rupees from C, and to lay it out on good security. B recovers the 1,00,000 rupees and lays out 90,000 rupees on good security, but lays out 10,000 rupees on security which he ought to have known to be bad, whereby A loses 2,000 rupees. B is entitled to remuneration for recovering the 1,00,000 rupees and for investing the 90,000 rupees. He is not entitled to any remuneration for investing the 10,000 rupees and he must make good the 2,000 rupees to B.

(b) A employs B to recover 1,000 rupees from C. Through B's misconduct the money is not recovered. B is entitled to no remuneration for his services, and must make good the loss.

**221.** In the absence of any contract to the contrary, an agent is entitled to retain goods, papers and other property, whether moveable, or immoveable, of the principal received by him, until the amount due to himself for commission, disbursements and services in respect of the same has been paid or accounted for to him.

Agent's lien on principal's property.

*Principal's Duty to Agent.*

Agent to be indemnified against consequences of lawful acts.

**222.** The employer of an agent is bound to indemnify him against the consequences of all lawful acts done by such agent in exercise of the authority conferred upon him.

*Illustrations.*

(a) B, at Singapore, under instructions from A of Calcutta, contracts with C to deliver certain goods to him. A does not send the goods to B, and C sues B for breach of contract. B informs A of the suit, and A authorizes him to defend the suit. B defends the suit, and is compelled to pay damages and costs, and incurs expenses. A is liable to B for such damages, costs and expenses.

(b) B, a broker at Calcutta, by the orders of A, a merchant there, contracts with C for the purchase of 10 casks of oil for A. Afterwards A refuses to receive the oil, and C sues B. B informs A, who repudiates the contract altogether. B defends, but unsuccessfully, and has to pay damages and costs and expenses.

**223.** Where one person employs another to do an act, and the agent does the act in good faith, the employer is liable to indemnify the agent against the consequences of that act, though it causes an injury to the rights of third persons.

Agent to be indemnified against consequence of acts done in good faith.

*Illustrations.*

(a) A, a decree-holder and entitled to execution of B's goods requires the officer of the Court to seize certain goods, representing them to be the goods of B. The officer seizes the goods, and is sued by C, the true owner of the goods. A is liable to indemnify the officer for the sum which he is compelled to pay to C, in consequence of obeying A's directions.

(b) B, at the request of A, sells goods in the possession of A, but which A had no right to dispose of. B does not know this, and hands over the proceeds of the sale to A. Afterwards C, the true owner of the goods, sues B and recovers the value of the goods and costs. A is liable to indemnify B for what he has been compelled to pay to C and for B's own expenses.

224. Where one person employs another to do an act which is criminal, the employer is not liable to

Non liability of employer of agent to do a criminal act.  
the agent, either upon an express or an implied promise, to indemnify him against the consequences of that act.

*Illustrations.*

(a) A employs B to beat C, and agrees to indemnify him against all consequences of the act. B thereupon beats C, and has to pay damages to C for so doing. A is not liable to indemnify B for those damages.

(b) B, the proprietor of a newspaper, publishes at A's request a libel upon C in the paper, and A agrees to indemnify B against the consequences of the publication, and all costs and damages of any action in respect thereof. B is sued by C and has to pay damages, and also incurs expenses. A is not liable to B upon the indemnity.

225. The principal must make compensation to his agent in respect of injury caused to such agent by the principal's neglect or want of skill.

Compensation to agent for injury caused by principal's neglect.

*Illustration.*

A employs B as a bricklayer in building a house, and puts up the scaffolding himself. The scaffolding is unskillfully put up, and B is in consequence hurt. A must make compensation to B.

*Effect of agency on contract with third persons.*

226. Contracts entered into through an agent and obligations arising from acts done by an agent, may be enforced in the same manner and will have the same legal consequences, as if the contracts had been entered into and the acts done by the principal in person.

*Illustrations.*

(a) A buys goods from B, knowing that he is an agent for their sale, but not knowing who is the principal. B's principal is the person entitled to claim from A the price of the goods, and A cannot, in a suit by the principal, set off against that claim a debt due to himself from B.

(b) A, being B's agent with authority to receive money on his behalf, receives from C a sum of money due to B. C is discharged of his obligation to pay the sum in question to B.

227. Where an agent does more than he is authorized to do, and when the part of what he does, which is within his authority, Principal how far bound when agent exceeds authority. can be separated from the part which is beyond his authority, so much only of what he does as is within his authority, is binding as between him and his principal.

*Illustration.*

A, being owner of a ship and cargo, authorizes B to procure an insurance for 4,000 rupees on the ship. B procures a policy for 4,000 rupees on the ship, and another for the like sum on the cargo. A is bound to pay the premium for the policy on the ship, but not the premium for the policy on the cargo.

**Principal not bound when excess of agent's authority is not separable.**

228. Where an agent does more than he is authorized to do, and what he does beyond the scope of his authority cannot be separated from what is within it, the principal is not bound to recognize the transaction.

*Illustration.*

A authorizes B to buy 500 sheep for him. B buys 500 sheep and 200 lambs for one sum of 6,000 rupees. A may repudiate the whole transaction.

229. Any notice given to or information obtained by the agent, provided it be given or obtained in the course of the business transacted by him for the principal, shall as between the principal, and third parties, have the same legal consequence as if it had been given to or obtained by the principal.

*Illustration.*

(a) A is employed by B to buy from C certain goods, of which C is the apparent owner, and buys them accordingly. In the course of the treaty for the sale, A learns that the goods really belonged to D, but B is ignorant of that fact. B is not entitled to set off a debt owing to him from C against the price of the goods.

(b) A is employed by B to buy from C goods of which C is the apparent owner. A was, before he was so employed, a servant of C, and then learnt that the goods really belonged to D, but B is ignorant of that fact. In spite of the knowledge of his agent, B may set off against the price of the goods a debt owing to him from C.

**Agent cannot personally enforce, nor be bound by, contracts on behalf of principal**

230. In the absence of any contract to that effect, an agent cannot personally enforce contracts entered into by him on behalf of his principal, nor is he personally bound by them.

**Presumption of contracts to contrary.**

Such a contract shall be presumed to exist in the following cases :-

- (1) where the contract is made by an agent for the sale or purchase of goods for a merchant resident abroad :
- (2) where the agent does not disclose the name of his principal :
- (3) where the principal, though disclosed, cannot be sued.

**231.** If an agent makes a contract with a person who neither knows, nor has reason to suspect, that he is an agent, his principal

**Rights of parties to a contract made by agent not disclosed** may require the performance of the contract ; but the other contracting party has, as against the principal, the same rights as he would have had as against the agent if the agent had been principal.

If the principal discloses himself before the contract is completed, the other contracting party may refuse to fulfil the contract, if he can show that, if he had known who was the principal in the contract, or if he had known that the agent was not a principal, he would not have entered into the contract.

**232** Where one man makes a contract with another, neither knowing nor having reasonable ground to suspect that the other is an agent, the principal, if he requires the performance of the contract, can only obtain such performance subject to the rights and obligations subsisting between the agent and the other party to the contract

#### *Illustration.*

A, who owes 500 rupees to B, sells 1,000 rupees' worth of rice to B. A is acting as agent for C in the transaction, but B has no knowledge nor reasonable ground of suspicion that such is the case. C cannot compel B to take the rice without allowing him to set off A's debt.

233. In cases where the agent is personally liable, a person dealing with him may hold either him or his principal, or both of them liable.

*Illustration.*

A enters into a contract with B to sell him 100 bales of cotton, and afterwards discovers that B was acting as agent for C. A may sue either B or C, or both, for the price of the cotton.

234. When a person who has made a contract with an agent induces the agent to act upon the belief that the principal only will be held liable, or induces the principal to act upon the belief that the agent only will be held liable, he cannot afterwards hold liable the agent or principal respectively.

Consequence of inducing agent or principal to act on behalf that principal or agent will be held exclusively liable.

235. A person untruly representing himself to be the authorized agent of another, and thereby inducing a third person to deal with him as such agent, is liable, if his alleged employer does not ratify his acts, to make compensation to the other in respect of any loss or damage which he has incurred by so dealing.

Liability of pretended agent.

236. A person with whom a contract has been entered into in the character of agent is not entitled to require the performance of it if he was in reality acting, not as agent, but on his own account.

Person falsely contracting as agent not entitled to performance.

237. When an agent has, without authority, done acts or incurred obligations to third persons on behalf of his principal, the principal is bound by such acts or obligations if he has by his words or conduct induced such third persons to believe that such acts and obligations were within the scope of the agent's authority.

Liability of principal inducing belief that agent's unauthorized acts were authorized.

*Illustrations.*

(a) A consigns goods to B for sale, and gives him instructions not to sell under a fixed price. C, being ignorant of B's instructions, enters into a contract with B to buy the goods at a price lower than the reserved price. A is bound by the contract.

(b) A entrusts B with negotiable instruments endorsed in blank. B sells them to C in violation of private orders from A. The sale is good.

238. Misrepresentations made, or frauds committed, by agents acting in the course of their business for their principals, have the

Effect, on agreement, of misrepresentation or fraud law, same effect on agreements made by such agents as if such misrepresentations or frauds had been made, or committed by the principal; but misrepresentations made, or frauds committed by agents, in matters which do not fall within their authority, do not affect their principals.

*Illustrations.*

(a) A being B's agent for the sale of goods, induces C to buy them by a misrepresentation, which he was not authorized by B to make. The contract is voidable, as between B and C at the option of C.

(b) A, the captain of B's ship, signs bills of lading without having received on board the goods mentioned therein. The bills of lading are void as between B and the pretended consignor.

# Indian Sale of Goods Act

## An Act to define and amend the law relating to the sale of goods

Whereas it is expedient to define and amend the law relating to the sale of goods ; it is hereby enacted as follows :

### CHAPTER I

#### Preliminary

1. (1) This Act may be called the Indian Sale of Goods Act, 1930.

**Short title, extent  
and commencement** (2) It extends to the whole of British India, including British Baluchistan and the North-Western Frontier Province.

(3) It shall come into force on the first day of July, 1930.

2. In this Act, unless there is anything repugnant in the subject or context,—

**Definitions** (1) "buyer" means a person who buys or agrees to buy goods;

(2) "delivery" means voluntary transfer of possession from one person to another;

(3) goods are said to be in a "deliverable state" when they are in such state that the buyer would, under the contract, be bound to take delivery of them;

(4) "document of title to goods" includes a bill of lading, dock-warrant, warehouse keeper's certificate, wharfingers' certificate, railway receipt, warrant or order for the delivery of goods and any other document used in the ordinary course of business as proof of the possession or control of goods, or authorising

or purporting to authorise, either by endorsement or by delivery, the possessor of the document to transfer or receive goods thereby represented ;

- (5) "fault" means wrongful act or default ;
- (6) "future goods" means goods to be manufactured or produced or acquired by the seller after the making of the contract of sale ;
- (7) "goods" means every kind of moveable property other than actionable claims and money ; and includes stock and shares, growing crops, grass, and things attached to or forming part of the land which are agreed to be severed before sale or under the contract of sale ;
- (8) a person is said to be "insolvent" who has ceased to pay his debts in the ordinary course of business, or cannot pay his debts as they become due, whether he has committed an act of insolvency or not ;
- (9) "mercantile agent" means a mercantile agent having in the customary course of business as such agent authority either to sell goods, or to consign goods for the purposes of sale, or to buy goods, or to raise money on the security of goods ;
- (10) "price" means the money consideration for a sale of goods ;
- (11) "property" means the general property in goods, and not merely a special property ;
- (12) "quality of goods" includes their state or condition ;
- (13) "seller" means a person who sells or agrees to sell goods ;
- (14) "specific goods" means goods identified and agreed upon at the time a contract of sale is made ; and
- (15) "expressions used but not defined in this Act and defined IX of 1872. in the Indian Contract Act, 1872, have the meanings assigned to them in that Act.

3. The unrepealed provisions of the Indian Contract Act,

*Application of provisions of Act IX of 1872.*

1872, save in so far as they are inconsistent with the express provisions of this Act, shall continue to apply to contracts for the sale of goods.

## CHAPTER II

### Formation of the Contract

#### *Contract of Sale.*

4. (1) A contract of sale of goods is a contract whereby the

*Sale and agreement to sell.* seller transfers or agrees to transfer the property in goods to the buyer for a price.

There may be a contract of sale between one part-owner and another.

(2) A contract of sale may be absolute or conditional.

(3) Where under a contract of sale the property in the goods is transferred from the seller to the buyer, the contract is called a sale, but where the transfer of the property in the goods is to take place at a future time or subject to some condition thereafter to be fulfilled, the contract is called an agreement to sell.

(4) An agreement to sell becomes a sale when the time elapses or the conditions are fulfilled subject to which the property in the goods is to be transferred.

#### *Formalities of the Contract.*

5. (1) A contract of sale is made by an offer to buy or sell goods for a price and the acceptance of such offer. The contract

*Contract of sale how made.* may provide for the immediate delivery of the goods or immediate payment of the price or both, or for the delivery or payment by instalments or delivery or payment or both shall be postponed.

(2) Subject to the provisions of any law for the time being

in force, a contract of sale may be made in writing or by word of mouth, or partly in writing and partly by word of mouth, or may be implied from the conduct of the parties.

### *Subject-matter of Contract*

6. (1) The goods which form the subject of a contract of Existing or future sale may be either existing goods, owned goods, or possessed by the seller, or future goods.

(2) There may be a contract for the sale of goods the acquisition of which by the seller depends upon a contingency which may or may not happen.

(3) Where by a contract of sale the seller purports to effect a present sale of future goods, the contract operates as an agreement to sell the goods.

7. Where there is a contract for the sale of specific goods, the contract is void if the goods without Goods perishing before making of contract the knowledge of the seller have, at the time when the contract was made, perished or become so damaged as no longer to answer to their description in the contract.

8. Where there is an agreement to sell specific goods, and subsequently the goods without any fault on the part of the seller or buyer perish or become so damaged as no longer to answer to their description in the agreement before the risk passes to the buyer, the agreement is thereby avoided. Goods perishing before sale but after agreement to sell.

### *The price.*

9. (1) The price in a contract of sale may be fixed by the contract or may be left to be fixed in manner thereby agreed or may be determined by the course of dealing between the parties. Ascertainment of price.

(2) Where the price is not determined in accordance with the foregoing provisions, the buyer shall pay the seller a reason-

able price. What is a reasonable price is a question of fact dependent on the circumstances of each particular case.

10. (1) Where there is an agreement to sell goods on the terms that the price is to be fixed by the valuation of a third party and such third party cannot or does not make such valuation, the agreement is thereby avoided:

Agreement to sell at valuation.  
Provided that, if the goods or any part thereof have been delivered to, and appropriated by, the buyer, he shall pay a reasonable price therefor.

(2) Where such third party is prevented from making the valuation by the fault of the seller or buyer, the party not in fault may maintain a suit for damages against the party in fault.

#### *Conditions and Warranties.*

11. Unless a different intention appears from the terms of Stipulations as to time of payment. the contract, stipulations as to time of payment are not deemed to be of the essence of a contract of sale. Whether any other stipulation as to time is of the essence of the contract or not depends on the terms of the contract.

Condition and warranty  
(1) A stipulation in a contract of sale with reference to goods which are the subject thereof may be a condition or a warranty.

(2) A condition is a stipulation essential to the main purpose of the contract, the breach of which gives rise to a right to treat the contract as repudiated.

(3) A warranty is a stipulation collateral to the main purpose of the contract, the breach of which gives rise to a claim for damages but not to a right to reject the goods and treat the contract as repudiated.

(4) Whether a stipulation in a contract of sale is a condition or a warranty depends in each case on the construction of the

contract. A stipulation may be a condition, though called a warranty in the contract.

13. (1) Where a contract of sale is subject to any condition to be fulfilled by the seller, the buyer may waive the condition or elect to treat the breach of the

When condition to be treated as warranty. condition as a breach of warranty and not as a ground for treating the contract as repudiated.

(2) Where a contract of sale is not severable and the buyer has accepted the goods or part thereof, or where the contract is for specific goods the property in which has passed to the buyer, the breach of any condition to be fulfilled by the seller can only be treated as a breach of warranty and not as a ground for rejecting the goods and treating the contract as repudiated, unless there is a term of the contract, express or implied, to that effect.

(3) Nothing in this section shall affect the case of any condition or warranty fulfilment of which is excused by law by reason of impossibility or otherwise.

14. In a contract of sale, unless the Implied undertaking circumstances of the contract are such as implying as to make it to show a different intention there is—

(a) an implied condition on the part of the seller that, in the case of a sale, he has a right to sell the goods and that, in the case of an agreement to sell, he will have a right to sell the goods at the time when the property is to pass;

(b) an implied warranty that the buyer shall have and enjoy quiet possession of the goods;

(c) an implied warranty that the goods shall be free from any charge or encumbrance in favour of any third party not declared or known to the buyer before or at the time when the contract is made.

15. Where there is a contract for the sale of goods by descrip-

tion, there is an implied condition that the goods shall correspond  
 Sale by description with the description ; and if the sale is by  
 sample as well as by description it is not  
 sufficient that the bulk of the goods corresponds with the sample  
 if the goods do not also correspond with the description

**16** Subject to the provisions of this Act and of any other Implied conditions law for the time being in force there is no as to quality or fit implied warranty or condition is to the quality or fitness for any particular purpose of goods supplied under a contract of sale except as follows —

(1) Where the buyer, expressly or by implication makes known to the seller the particular purpose for which the goods are required, so as to show that the buyer relies on the seller's skill or judgment, and the goods are of a description which it is in the course of the seller's business to supply (whether he is the manufacturer or producer or not), there is an implied condition that the goods shall be reasonably fit for such purpose.

Provided that, in the case of a contract for the sale of a specified article under its patent or other trade name, there is no implied condition as to its fitness for any particular purpose.

(2) Where goods are bought by the description from a seller who deals in goods of that description (whether he is the manufacturer or producer or not) there is an implied condition that the goods shall be of merchantable quality.

Provided that, if the buyer has examined the goods, there shall be no implied condition as regards defects which such examination ought to have revealed.

(3) An implied warranty or condition as to quality or

fitness for a particular purpose may be annexed by the usage of trade.

- (4) An express warranty or condition does not negative a warranty or condition implied by this Act unless inconsistent therewith.
17. (1) A contract of sale is a contract for sale by sample where there is a term in the contract, express or implied, to that effect.
- Sale by sample.
- (2) In the case of a contract for sale by sample there is an implied condition—
- (a) that the bulk shall correspond with the sample in quality;
  - (b) that the buyer shall have a reasonable opportunity of comparing the bulk with the sample;
  - (c) that the goods shall be free from any defect, rendering them unmerchantable, which would not be apparent on reasonable examination of the sample.

### CHAPTER III

#### Effects of the Contract

*Transfer of property as between seller and buyer.*

18. Where there is a contract for the sale of unascertained goods, no property in the goods is transferred to the buyer unless and until the goods are ascertained.
- Goods must be ascertained.
- Property passes when intended to pass.
19. (1) Where there is a contract for the sale of specific or ascertained goods the property in them is transferred to the buyers at such time as the parties to the contract intend it to be transferred.

- (2) For the purpose of ascertaining the intention of the parties regard shall be had to the terms of the contract, the conduct of the parties and the circumstances of the case.

(3) Unless a different intention appears, the rules contained in sections 20 to 24 are rules for ascertaining the intention of the parties as to the time at which the property in the goods is to pass to the buyer.

20. Where there is an unconditional contract for the sale of specific goods in a deliverable state, the property in the goods

**Specific goods in a deliverable State.** passes to the buyer when the contract is made, and it is immaterial whether the time of payment of the price or the time of delivery of the goods, or both, is postponed.

21. Where there is a contract for the sale of specific goods and the seller is bound to do something to the goods for the purpose of putting them into a deliverable state, the property does not pass until such thing is done and the

**Specific goods to be put into a deliverable state.** buyer has notice thereof.

22. Where there is a contract for the sale of specific goods in a deliverable state, but the seller is bound to weigh, measure, test or do some other act or thing with reference to the goods for the purpose of ascertaining the price, the property does not pass until such act or thing is done and the buyer has notice therenf.

**Specific goods in a deliverable state, when the seller has to do anything thereto in order to ascertain price.**

23. (1) Where there is a contract for the sale of unascertained or future goods by description and goods of that description and in a deliverable state are unconditionally appropriated to the contract, either by the seller with the assent of the buyer or by the buyer with the assent of the seller.

**Sale of unascertained goods and appropriation.** the property in the goods thereupon passes to the buyer. Such assent may be express or implied, and may be given either before or after the appropriation is made.

(2) Where, in pursuance of the contract, the seller delivers the goods to the buyer or to a carrier or other bailee (whether named by the buyer or not) for the purpose of transmission to the buyer, and doe-

not reserve the right of disposal, he is deemed to have unconditionally appropriated in goods to the contract.

Goods sent on approval or "on sale or return"

24. When goods are delivered to the buyer on approval or 'on sale or return' or other similar terms, the property therein passes to the buyer—

- (a) when he signifies his approval or acceptance to the seller or does any other act adopting the transaction;
- (b) if he does not signify his approval or acceptance to the seller but retains the goods without giving notice of rejection, then, if a time has been fixed for the return of the goods, on the expiration of such time, and, if no time has been fixed, on the expiration of a reasonable time

25 (1) Where there is a contract for the sale of specific goods or where goods are subsequently appropriated to the contract, the seller may, by the terms of the

*Reservation of right of disposal* contract or appropriation, reserve the right of disposal of the goods until certain conditions are fulfilled. In such case, notwithstanding the delivery of the goods to a buyer, or to a carrier or other bailee for the purpose of transmission to the buyer, the property in the goods does not pass to the buyer until the conditions imposed by the seller are fulfilled

(2) Where goods are shipped and by the bill of lading the goods are deliverable to the order of the seller or his agent, the seller is *prima facie* deemed to reserve the right of disposal.

(3) Where the seller of goods draws on the buyer for the price and transmits the bill of exchange and bill of lading to the buyer together, to secure acceptance or payment of the bill of exchange, the buyer is bound to return the bill of lading if he does not honour the bill of exchange and if he wrongfully retains the bill of lading the property in the goods does not pass to him.

26. Unless otherwise agreed, the goods remain at the seller's risk until the property therein is transferred to the buyer, but when the property therein is transferred to the buyer, the goods are at the buyer's risk <sup>Risk prima facie passes with property</sup> whether delivery has been made or not :

Provided that, where delivery has been delayed through the fault of either buyer or seller, the goods are at the risk of the party in fault as regards any loss which might not have occurred but for such fault

Provided also that nothing in this section shall affect the duties or liabilities of either seller or buyer as a bailee of the goods of the other party.

#### *Transfer of title*

27 Subject to the provisions of this Act and of any other law for the time being in force, where goods are sold by a person who is not the owner thereof and who does not sell them under the authority or with the consent of the owner, the buyer acquires no better title to the goods than the seller had, unless the owner of the goods is by his conduct precluded from denying the seller's authority to sell

Provided that, where a mercantile agent is, with the consent of the owner, in possession of the goods or of the goods or of document of title to the goods, any sale made by him, when acting in the ordinary course of a mercantile agent, shall be as valid as if he were expressly authorised by the owner of the goods to make the same, provided that the buyer acts in good faith and has not at the time of the contract of sale notice that the seller has not authority to sell

28 If one of several joint owners of goods has the sole possession of them by permission of the co-owners, the property in the goods is transferred to any person who buys them of such joint

<sup>Sale by one of joint owners</sup>

owner in good faith and has not at the time of the contract of sale notice that the seller has not authority to sell.

**29. When the seller of goods has obtained possession thereof under a contract voidable under section 19 or section 19A of the Indian Contract Act, 1872,**

**Sale by person in possession under voidable contract IX of 1872 .** but the contract has not been rescinded at the time of the sale, the buyer acquires a good title to the goods, provided he buys them in good faith and without notice of the seller's defect of title.

**30. (1) Where a person, having sold goods, continues or is in possession of the goods or of the documents of title to the goods, the delivery or transfer by that person or by a mercantile agent acting for him, of the goods or documents of title under any sale, pledge or other disposition**

**Seller or buyer in possession after sale.** thereof to any person receiving the same in good faith and without notice of the previous sale shall have the same effect as if the person making the delivery or transfer were expressly authorised by the owner of the goods to make the same.

**(2) Where a person, having bought or agreed to buy goods, obtains, with the consent of the seller, possession of the goods or the documents of title to the goods, the delivery or transfer by that person or by a mercantile agent acting for him, of the goods or documents of title under any sale, pledge or other disposition thereof to any person receiving the same in good faith and without notice of any lien or other right of the original seller in respect of the goods shall have effect as if such lien or right did not exist.**

## CHAPTER IV

### Performance of the Contract

31. It is the duty of the seller to deliver the goods and of the buyer to accept and pay for them, in accordance with the terms of the contract of sale.

32. Unless otherwise agreed, delivery of the goods and payment of the price are concurrent conditions, that is to say, the seller shall be ready and willing to give possession of the goods to the buyer in exchange for the price, and the buyer shall be ready and willing to pay the price in exchange for possession of the goods.

33. Delivery of goods sold may be made by doing anything which the parties agree shall be treated as delivery or which has the effect of putting the goods in the possession of the buyer or of any person authorised to hold them on his behalf.

34. A delivery of part of goods, in progress of the delivery of the whole, has the same effect, for the purpose of passing the property in such goods, as a delivery of the whole : but a delivery of part of the goods with an intention of severing it from the whole, does not operate as a delivery of the remainder.

35. Apart from any express contract, the seller of goods is not bound to deliver them until the buyer applies for delivery.

36. (1) Whether it is for the buyer to take possession of the goods or for the seller to send them to the buyer is a question depending in each case on the contract.

Rules as to delivery. Express or implied, between the parties. Apart from any such contract, goods sold are to be delivered at the place at which they are at the time of the sale, and goods agreed to be sold are to be delivered at the place at which they

are at the time of the agreement to sell, or, if not then in existence, at the place at which they are manufactured or produced.

(2) Where under the contract of sale the seller is bound to send the goods to the buyer, but no time for sending them is fixed, the seller is bound to send them within a reasonable time.

(3) Where the goods at the time of sale are in the possession of a third person, there is no delivery by seller to buyer unless and until such third person acknowledges to the buyer that he holds the goods on his behalf :

Provided that nothing in this section shall affect the operation of the issue or transfer of any document of title to goods.

(4) Demand or tender of delivery may be treated as ineffectual unless made at a reasonable hour. What is a reasonable hour is a question of fact.

(5) Unless otherwise agreed, the expenses of and incidental to putting the goods into a deliverable state shall be borne by the seller.

37. (1) Where the seller delivers to the buyer a quantity of goods less than he contracted to sell, the buyer may reject them, but if the buyer accepts the goods so delivered he shall pay for them at the contract rate.  
Delivery of wrong quantity.

(2) Where the seller delivers to the buyer a quantity of goods larger than he contracted to sell, the buyer may accept the goods included in the contract and reject the rest, or he may reject the whole. If the buyer accepts the whole of the goods so delivered, he shall pay for them at the contract rate.

(3) Where the seller delivers to the buyer the goods he contracted to sell mixed with goods of a different description not included in the contract, the buyer may accept the goods which are in accordance with the contract and reject the rest, or may reject the whole.

(4) The provisions of this section are subject to any usage of trade, special agreement or course of dealing between the parties

38. (1) Unless otherwise agreed, the buyer of goods is not bound to accept delivery thereof by instalments.

Instalment delivery (2) Where there is a contract for the sale of goods to be delivered by stated instalments which are to be separately paid for, and the seller makes no delivery or defective delivery in respect of one or more instalments, or the buyer neglects or refuses to take delivery of or pay for one or more instalments, it is a question in each case depending on the contract and the circumstances of the case, whether the breach of contract is a repudiation of the whole contract, or whether it is a severable breach giving rise to a claim for compensation, but not to a right to treat the whole contract as repudiated.

39. (1) Where, in pursuance of a contract of sale, the seller is authorised or required to send the goods to the buyer, delivery of the goods to a carrier, whether named Delivery to carrier or wharfinger. by the buyer or not, for the purpose of transmission to the buyer, or delivery of the goods to a wharfinger for safe custody, is *prima facie* deemed to be a delivery of the goods to the buyer.

(2) Unless otherwise authorised by the buyer, the seller shall make such contract with the carrier or wharfinger on behalf of the buyer as may be reasonable having regard to the nature of the goods and the other circumstances of the case. If the seller omits so to do, and the goods are lost or damaged in course of transit or whilst in the custody of the wharfinger, the buyer may decline to treat the delivery to the carrier or wharfinger as a delivery to himself, or may hold the seller responsible in damages.

(3) Unless otherwise agreed, where goods are sent by the seller to the buyer by a route involving sea transit, in circumstances in which it is usual to insure, the seller shall give such notice to the buyer as may enable him to insure them during their sea transit, and if the seller fails so to do, the goods shall be deemed to be at his risk during such sea transit.

40. Where the seller of goods agrees to deliver them at his own risk at a place other than that where they are when sold, the buyer shall, nevertheless, unless otherwise agreed, take any risk of deterioration in the goods necessarily

Risk where goods  
are delivered at dis-  
tant place.

incident to the course of transit.

41. (1) Where goods are delivered to the buyer which he has not previously examined, he is not deemed to have accepted them unless and

Buyer's right of  
examining the goods.

until he has had a reasonable opportunity of examining them for the purpose of ascertaining whether they are in conformity with the contract.

(2) Unless otherwise agreed, when the seller tenders delivery of goods to the buyer, he is bound, on request, to afford the buyer a reasonable opportunity of examining the goods for the purpose of ascertaining whether they are in conformity with the contract.

42. The buyer is deemed to have accepted the goods when he intimates to the seller that he has accepted them, or when the goods have been delivered to him and

Acceptance

he does any act in relation to them which is inconsistent with the ownership of the seller, or when, after the lapse of reasonable time, he retains the goods without intimating to the seller that he has rejected them.

43. Unless otherwise agreed, where goods are delivered to the buyer and he refuses to accept them,

Buyer not bound to  
return rejected goods

having the right so to do, he is not bound to return them to the seller, but it is sufficient if he intimates to the seller that he refuses to accept them.

44. When the seller is ready and willing to deliver the goods and request the buyer to take delivery, and the buyer does not

Liability of buyer  
for neglecting or re-  
fusing delivery of  
goods.

within a reasonable time after such request take delivery of the goods, he is liable to the seller for any loss occasioned by his neglect or refusal to take delivery, and also

for a reasonable charge for the care and custody of the goods :

Provided that nothing in this section shall affect the rights of the seller where the neglect or refusal of the buyer to take delivery amounts to a repudiation of the contract.

## CHAPTER V

### Rights of Unpaid Seller against the Goods

45. (1) The seller of goods is deemed "Unpaid seller" to be an "unpaid seller" within the meaning of this Act—

(a) when the whole of the price has not been paid or tendered;

(b) when a bill of exchange or other negotiable instrument has been received as conditional payment, and the condition on which it was received has not been fulfilled by reason of the dishonour of the instrument or otherwise.

(2) In this Chapter, the term "seller" includes any person who is in the position of a seller, as, for instance, an agent of the seller to whom the bill of lading has been indorsed, or a consignor or agent who has himself paid, or is directly responsible for, the price.

46. (1) Subject to the provisions of this Act and of any law for the time being in force, notwithstanding Unpaid seller's rights that the property in the goods may have passed to the buyer, the unpaid seller of goods, as such, has by implication of law—

(a) a lien on the goods for the price while he is in possession of them;

(b) in case of the insolvency of the buyer a right of stopping the goods in transit after he has parted with the possession of them;

(c) a right of re-sale as limited by this Act.

(2) Where the property in goods has not passed to the buyer the unpaid seller has, in addition to his other remedies, a right of

withholding delivery similar to and co-extensive with his rights of lien and stoppage in transit where the property has passed to the buyer.

*Unpaid seller's lien.*

47. (1) Subject to the provisions of this Act, the unpaid seller of goods who is in possession of them is entitled to retain possession of them until payment or tender of the price in the following cases, namely :—

(a) where the goods have been sold without any stipulation as to credit ;

(b) where the goods have been sold on credit, but the term of credit has expired ;

(c) where the buyer becomes insolvent.

(2) The seller may exercise his right of lien notwithstanding that he is in possession of the goods as agent or bailee for the buyer.

48. Where an unpaid seller has made part delivery of the goods, he may exercise his right of lien on the remainder, unless Part delivery. such part delivery has been made under such circumstances as to show an agreement to waive the lien.

49. (1) The unpaid seller of goods loses his lien thereon—

(a) when he delivers the goods to a carrier or other bailee for the purpose of transmission to the buyer without reserving the right of disposal of the goods ;

(b) when the buyer or his agent lawfully obtains possession of the goods ;

(c) by waiver thereof.

(2) The unpaid seller of goods, having lien thereon, does not lose his lien by reason only that he has obtained a decree for the price of the goods.

*Stoppage in transit.*

50. Subject to the provisions of the Act, when the buyer of

goods becomes insolvent, the unpaid seller who has parted with the possession of the goods has the right of stopping them in transit, that is to say, he may resume possession of the goods as long as they are in the course of transit, and may retain them until payment or tender of the price.

**Right of stoppage in transit**

51. (1) Goods are deemed to be in course of transit from the time when they are delivered to a carrier or other bailee for the purpose of transmission to the buyer, until the buyer or his agent in that behalf takes delivery of them from such carrier or other bailee.

(2) If the buyer or his agent in that behalf obtains delivery of the goods before their arrival at the appointed destination the transit is at an end.

(3) If, after the arrival of the goods at the appointed destination, the carrier or other bailee acknowledges to the buyer or his agent that he holds the goods on his behalf and continues in possession of them as bailee for the buyer or his agent, the transit is at an end and it is immaterial that a further destination for the goods may have been indicated by the buyer.

(4) If the goods are rejected by the buyer and the carrier or other bailee continues in possession of them, the transit is not deemed to be at an end even if the seller has refused to receive them back.

(5) When goods are delivered to a ship chartered by the buyer, it is a question depending on the circumstances of the particular case whether they are in the possession of the master as a carrier or as agent of the buyer.

(6) Where the carrier or other bailee wrongfully refuses to deliver the goods to the buyer or his agent in that behalf, the transit is deemed to be at an end.

(7) Where part delivery of the goods has been made to the buyer or his agent in that behalf, the remainder of the goods may be stopped in transit, unless such part delivery has been given in

such circumstances as to show an agreement to give up possession of the whole of the goods.

52. (1) The unpaid seller may exercise his right of stoppage in transit either by taking actual possession of the goods, or by giving notice of his claim to the carrier or other bailee in whose possession the goods are. Such notice may be given either to the person in actual possession of the goods or to his principal. In the latter case the notice, to be effectual, shall be given at such time and in such circumstances that the principal, by the exercise of reasonable diligence, may communicate it to his servant or agent in time to prevent a delivery to the buyer.

(2) When notice of stoppage in transit is given by the seller to the carrier or other bailee in possession of the goods, he shall re-deliver the goods to, or according to the direction of, the seller. The expenses of such re-delivery shall be borne by the seller.

#### *Transfer by buyer and seller*

53. (1) Subject to the provisions of this act, the unpaid seller's right of lien or stoppage in transit is not affected by any sale or other disposition of the goods which the buyer may have made, unless the seller has assented thereto:

Provided that where a document of title to goods has been issued or lawfully transferred to any person as buyer or owner of the goods, and that person transfers the document to a person who takes the document in good faith and for consideration, then, if such last mentioned transfer was by way of sale, the unpaid seller's right of lien or stoppage in transit is defeated, and, if such last mentioned transfer was by way of pledge or other disposition for value, the unpaid seller's right of lien or stoppage in transit can only be exercised subject to the rights of the transferee.

(2) Where the transfer is by way of pledge, the unpaid seller may require the pledge to have the amount secured by the pledge satisfied in the first instance, as far as possible, out of any other

**goods or securities of the buyer in the hands of the pledgee and available against the buyer.**

**Sale not generally rescinded by lien or stoppage in transit.**

54. (1) Subject to the provisions of this section, a contract of sale is not rescinded by the mere exercise by an unpaid seller of his right of lien or stoppage in transit.

(2) Where the goods are of a perishable nature, or where the unpaid seller who has exercised his right of lien or stoppage in transit gives notice to the buyer of his intention to re-sell, the unpaid seller may, if the buyer does not, within a reasonable time, pay or tender the price, re-sell the goods within a reasonable time and recover from the original buyer damages for any loss occasioned by his breach of contract, but the buyer shall not be entitled to any profit which may occur on the re-sale. If such notice is not given, the unpaid seller shall not be entitled to recover such damages and the buyer shall be entitled to the profit, if any, on the re-sale.

(3) Where an unpaid seller who has exercised his right of lien or stoppage in transit re-sells the goods, the buyer acquires a good title thereto as against the original buyer, notwithstanding that no notice of the re-sale has been given to the original buyer

(4) Where the seller expressly reserves a right of re-sale in case the buyer should make default, and, on the buyer making default, re-sells the goods, the original contract of sale is thereby rescinded, but without prejudice to any claim which the seller may have for damages.

## CHAPTER VI

### Suits for Breach of the Contract

55. (1) Where under a contract of the sale the property in the goods has passed to the buyer and the buyer wrongfully neglects or refuses to pay for the goods

**Suit for price.** according to terms of the contract, the seller may sue him for the price of the goods.

(2) Where under a contract of sale the price is payable on a certain day irrespective of delivery and the buyer wrongfully neglects or refuses to pay such price, the seller may sue him for the price although the property in the goods has not passed and the goods have not been appropriated to the contract.

Damages for acceptance.

56. Where the buyer wrongfully neglects or refuses to accept and pay for the goods, the seller may sue him for damages for non-acceptance.

Damages for non-delivery.

57. Where the seller wrongfully neglects or refuses to deliver the goods to the buyer the buyer may sue the seller for damages for non-delivery.

58. Subject to the provisions of Chapter II of the Specific Relief Act, 1877, in any suit for breach of contract to deliver specific or ascertained goods, the Court

Specific performance.  
may, if it thinks fit, on the application of the plaintiff, by its decree direct that the contract shall be performed specifically, without giving the defendant the option of retaining the goods on payment of damages. The decree may be unconditional, or upon such terms and conditions as to damages, payment of the price or otherwise, as the Court may deem just, and the application of the plaintiff may be made at any time before the decree.

59. (1) Where there is a breach of warranty by the seller, or where the buyer elects or is compelled Remedy for breach of warranty. to treat any breach of condition on the part of the seller as breach of warranty, the buyer is not by reason only of such breach of warranty entitled to reject the goods; but he may—

(a) set up against the seller the breach of warranty in diminution or extinction of the price; or

(b) sue the seller for damages for breach of warranty.

(2) The fact that a buyer has set up a breach of warranty in diminution or extinction of the price does not prevent him from

suing for the same breach of warranty if he has suffered further damage.

**60. Where either party to a contract of sale repudiates the contract before the date of delivery,** the other may either treat the contract as subsisting and wait till the date of delivery, or he may treat the contract as rescinded and sue for damages for the breach.

**61. (1) Nothing in this Act shall affect the right of the seller or the buyer to recover interest or special damages in any case where by law interest or special damages may be recoverable, or to recover the money paid where the consideration for the payment of it has failed.**

**(2) In the absence of a contract to the contrary, the Court may award interest at such rate as it thinks fit on the amount of the price—**

- (a) to seller in a suit by him for the amount of the price—from the date of the tender of the goods or from the date on which the price was payable;**
- (b) to the buyer in a suit by him for the refund of the price in a case of breach of the contract on the part of the seller—from the date on which the payment was made.**

## CHAPTER VII

### Miscellaneous

**62. Where any right, duty or liability would arise under a contract of sale by implication of law, it may be negatived or varied by express agreement or by the course of dealing between the parties, or by usage, if the usage is such as to bind both parties to the contract.**

**Reasonable time  
a question of  
fact.**

63. Where in this Act any reference is made to a reasonable time, the question what is a reasonable time is a question of fact.

**Auction sale.**

64. In the case of a sale by auction—

- (1) where goods are put up for sale in lots, each lot is *prima facie* deemed to be the subject of a separate contract of sale;
- (2) the sale is complete when the auctioneer announces its completion by the fall of the hammer or in other customary manner; and, until such announcement is made, any bidder may retract his bid;
- (3) a right to bid may be reserved expressly by or on behalf of the seller and, where such right is expressly so reserved, but not otherwise, the seller or any one person on his behalf may, subject to the provisions hereinafter contained, bid at the auction;
- (4) where the sale is not notified to be subject to a right to bid on behalf of the seller, it shall not be lawful for the seller to bid himself or to employ any person to bid at such sale, or for the auctioneer knowingly to take any bid from the seller or any such person; and any sale contravening this rule may be treated as fraudulent by the buyer;
- (5) the sale may be notified to be subject to a reserved or upset price;
- (6) if the seller makes use of pretended bidding to raise the price, the sale is voidable at the option of the buyer.

**Repeal.** 65. Chapter VII of the Indian Contract Act, 1872, is hereby repealed.

**Savings.** 66. (1) Nothing in this Act or in any repeal effected thereby shall affect or be deemed to affect—

- (a) any right, title, interest, obligation or liability already acquired, accrued or incurred before the commencement of this Act, or
- (b) any legal proceedings or remedy in respect of any such right, title, interest, obligation or liability, or
- (c) anything done or suffered before the commencement of

- (d) any enactment relating to the sale of goods which is not expressly repealed by this Act, or
  - (e) any rule of law not inconsistent with this Act.
- (2) The rules of insolvency relating to contracts for the sale of goods shall continue to apply thereto, notwithstanding anything contained in this Act.
- (3) The provisions of this Act relating to contracts of sale do not apply to any transaction in the form of a contract of sale which is intended to operate by way of mortgage, pledge, charge or other security.

# The Indian Partnership Act, 1932

## (IX of 1932)

[Passed by the Indian Legislature]

(Received the assent of the Governor-General on the  
8th April, 1932.)

An Act to define and amend the law relating to partnership.

Whereas it is expedient to define and amend the law relating to partnership ; It is hereby enacted as follows :—

### CHAPTER I.

#### Preliminary

**Short title, extent and commencement.** 1. (i) This Act may be called the Indian Partnership Act, 1932.

(ii) It extends to the whole of British India, including British Baluchistan and the Sonthal Parganas.

(iii) It shall come into force on the 1st day of October, 1932, except section 69, which shall come into force on the 1st day of October, 1933.

**Definitions.** 2. In this Act, unless there is anything repugnant in the subject or context,—

(a) an "act of a firm" means any act or omission by all the partners, or by any partner or agent of the firm which gives rise to a right enforceable by or against the firm ;

(b) "business" includes every trade, occupation and profession ;

(c) "prescribed" means prescribed by rules made under this Act ;

(d) "third party" used in relation to a firm or to a partner therein means any person who is not a partner in the firm ; and

(e) expressions used but not defined in this Act, and defined in the Indian Contract Act, 1872, shall have the meanings assigned to them in that Act.

**Application of provisions of Act IX of 1872.** 3. The unrepealed provisions of the Indian Contract Act, 1872, save in so far as they are inconsistent with the express provisions of this Act, shall continue to apply to firms.

## CHAPTER II.

### The Nature of Partnership

**Definition of "partnership", "partner", "firm" and "firm name"**

4. "Partnership" is the relation between persons who have agreed to share the profits of a business carried on by all or any of them acting for all.

Persons who have entered into partnership with one another are called individually "partners" and collectively "a firm", and the name under which their business is carried on is called the "firm name."

**Partnership not created by status.** 5. The relation of partnership arises from contract and not from status ; and, in particular, the members of a Hindu undivided family carrying on a family business as such, or a Burmese Buddhist husband and wife carrying on business as such, are not partners in such business.

**Mode of determining existence of partnership.** 6. In determining whether a group of persons is or is not a firm, or whether a person is or is not a partner in a firm, regard shall be had to the real relation between the parties, as shown by all relevant facts taken together.

*Explanation 1.*—The sharing of profits or of gross returns arising from property by persons holding a joint or common interest in that property does not of itself make such persons partners.

*Explanation 2.*—The receipt by a person of a share of the profits of a business, or of a payment contingent upon the earning of profits or varying with the profits earned by a business, does

not of itself make him a partner with the persons carrying on the business;

- and, in particular, the receipt of such share or payment--
- (a) by a lender of money to persons engaged or about to engage in any business,
  - (b) by a servant or agent as remuneration,
  - (c) by the widow or child of a deceased partner, as annuity, or
  - (d) by a previous owner or part owner of the business, as consideration for the sale of the goodwill or share thereof,

does not of itself make the receiver a partner with the persons carrying on the business.

7. Where no provision is made by contract between the Partnership partners for the duration of their partnership, or at will. for the determination of their partnership, the partnership, is "partnership at will."

**Particular partnership.** 8. A person may become a partner with another person in particular adventures or undertakings

### CHAPTER III

#### Relation of Partners to one another

9. Partners are bound to carry on the business of the firm to the greatest common advantage, to be just and faithful to each other, and to render true accounts and full information of all things affecting the firm to any partner or his legal representative.

**Duty to indemnify for loss caused by fraud.** 10. Every partner shall indemnify the firm for any loss caused to it by his fraud in the conduct of the business of the firm.

11. (i) Subject to the provisions of this Act, the mutual rights and duties of the partners of a firm may be determined by contract between the partners, and such contract may be express or may be implied by a course of dealing.

Such contract may be varied by consent of all the partners,

and such consent may be express or may be implied by a course of dealing.

(ii) Notwithstanding anything contained in section 27 of the Agreements in Indian Contract Act, 1872, such contracts may restrain of provide that a partner shall not carry on any trade. business other than that of the firm while he is a partner.

The conduct of 12. Subject to contract between the the business partners—

- (a) every partner has a right to take part in the conduct of the business ;
- (b) every partner is bound to attend diligently to his duties in the conduct of the business ;
- (c) any difference arising as to ordinary matters connected with the business may be decided by a majority of the partners, and every partner shall have the right to express his opinion before the matter is decided but no change may be made in the nature of the business without the consent of all the partners ; and
- (d) every partner has a right to have access to and to inspect and copy any of the books of the firm.

Mutual rights 13. Subject to contract between the and liabilities. partners -

- (a) a partner is not entitled to receive remuneration for taking part in the conduct of the business ;
- (b) the partners are entitled to share equally in the profits earned, and shall contribute equally to the losses sustained by the firm ;
- (c) where a partner is entitled to interest on the capital subscribed by him such interest shall be payable only out of profits ;
- (d) a partner making, for the purposes of the business, any payment or advance beyond the amount of capital he has agreed to subscribe, is entitled to interest thereon at the rate of six per cent. per annum ;
- (e) the firm shall indemnify a partner in respect of payments made and liabilities incurred by him—
  - (i) in the ordinary and proper conduct of the business, and
  - (ii) in doing such act, in an emergency, for the purpose

of protecting the firm from loss, as would be done by a person of ordinary prudence, in his own case, under similar circumstances ; and

- (f) a partner shall indemnify the firm for any loss caused to it by his wilful neglect in the conduct of the business of the firm.

**14. Subject to contract between the partners,** the property of the firm includes all property and rights and interests in property originally brought into the stock of the firm, or acquired, by purchase or otherwise, by or for the firm, or for the purposes and in the course of the business of the firm, and includes also the goodwill of the business.

**The property of the firm.** Unless the contrary intention appears, property and rights and interests in property acquired with money belonging to the firm are deemed to have been acquired for the firm.

**Application of the property of the firm.** **15. Subject to contract between the partners,** the property of the firm shall be held and used by the partners exclusively for the purposes of the business.

**Personal profits earned by partners.** **16. Subject to contract between the partners, —**

- (a) if a partner derives any profit for himself from any transaction of the firm, or from the use of the property or business connection of the firm or the firm name, he shall account for that profit and pay it to the firm ;
- (b) if a partner carries on any business of the same nature as and competing with that of the firm, he shall account for and pay to the firm all profits made by him in that business.

**17. Subject to contract between the partners, —**

**Rights and duties of partners after a change in the firm.** (a) where a change occurs in the constitution of a firm, the mutual rights and duties of the partners in the reconstituted firm remain the same as they were immediately before the change, as far as may be;

**After the expiry of the term of the firm, and** (b) where a firm constituted for a fixed term continues to carry on business after the expiry of that term, the mutual rights and duties of the partners remain the same as they were before the expiry,

so far as they may be consistent with the incidents of partnership at will ; and

(c) where a firm constituted to carry out one or more where additional adventures or undertakings carries out other undertakings are carried out. duties of the partners in respect of the other adventures or undertakings are the same as those in respect of the original adventures or undertakings.

## CHAPTER IV

### Relations of Partners to Third parties

**Partner to be agent of the firm.** 18. Subject to the provisions of this Act, a partner is the agent of the firm for the purposes of the business of the firm.

**Implied authority of partner as agent of the firm.** 19. (i) Subject to the provisions of section 22, the act of a partner which is done to carry on, in the usual way, business of the kind carried on by the firm, binds the firm.

The authority of a partner to bind the firm conferred by this section is called his "implied authority."

(ii) In the absence of any usage or custom of trade to the contrary, the implied authority of a partner does not empower him to

- (a) submit dispute relating to the business of the firm to arbitration,
- (b) open a banking account on behalf of the firm in his own name,-
- (c) compromise or relinquish any claim or portion of a claim by the firm, . . ,
- (d) withdraw a suit or proceeding filed on behalf of the firm, .
- (e) admit any liability in a suit or proceeding against the firm, .
- (f) acquire immoveable property on behalf of the firm,
- (g) transfer immoveable property belonging to the firm, or
- (h) enter into partnership on behalf of the firm. . .

**Extension and restriction of partner's implied authority.**

20. The partners in a firm may, by contract between the partners, extend or restrict the implied authority of any partner.

Notwithstanding any such restriction, any act done by a partner on behalf of the firm which falls within his implied authority binds the firm, unless the person with whom he is dealing knows of the restriction or does not know or believe that partner to be a partner.

**Partner's authority in an emergency.** 21. A partner has authority, in an emergency, to do all such acts for the purpose of protecting the firm from loss as would be done by a person of ordinary prudence, in his own case, acting under similar circumstances, and such acts bind the firm.

**Mode of doing act to bind firm.** 22. In order to bind a firm, an act or instrument done or executed by a partner or other person on behalf of the firm shall be done or executed in the firm name, or in any other manner expressing or implying an intention to bind the firm.

**Effect of admissions by a partner.** 23. An admission or representation made by a partner concerning the affairs of the firm is evidence against the firm, if it is made in the ordinary course of business.

**Effect of notice to acting partner.** 24. Notice to a partner who habitually acts in the business of the firm of any matter relating to the affairs of the firm operates as notice to the firm, except in the case of a fraud on the firm committed by or with the consent of that partner.

**Liability of a partner for acts of the firm.** 25. Every partner is liable, jointly with all the other partners and also severally, for all acts of the firm done while he is a partner.

**Liability of the firm for wrongful acts of a partner.** 26. Where, by the wrongful act or omission of a partner acting in the ordinary course of the business of a firm, or with the authority of his partners, loss or injury is caused to any third party, or any penalty is incurred, the firm is liable therefor to the same extent as the partner.

**Liability of firm for misapplication by partners.** 27. Where—  
(a) a partner acting with his apparent authority receives money or property from a third party and misapplies it, or

(3) a firm in the course of its business receives money or property from a third party, and the money or property is misapplied by any of the partners while it is in the custody of the firm, the firm is liable to make good the loss.

28. (i) Any one who by words spoken or written or by conduct represents himself, or knowingly permits himself to be represented, to be a partner in a firm, is liable as a partner in that firm to any one who has on the faith of any such holding out representation given credit to the firm, whether the person representing himself or represented to be partner does or does not know that the representation has reached the person so giving credit.

(ii) Where after a partner's death the business is continued in the old firm name, the continued use of that name or of the deceased partner's name as a part thereof shall not of itself make his legal representative or his estate liable for any act of the firm done after his death.

29. (1) A transfer by partner of his interest in the firm, either absolute or by mortgage, or by the creation by him of a charge on such interest, does not entitle the transferee of a partner's interest to interfere in the conduct of the business, or to require accounts, or to inspect the books of the firm, but entitles the transferee only to receive the share of profits of the transferring partner, and the transferee shall accept the account of profits agreed to by the partners.

(2) If the firm is dissolved or if the transferring partner ceases to be partner, the transferee is entitled as against the remaining partners to receive the share of the assets of the firm to which the transferring partner is entitled, and, for the purpose of ascertaining that share, to an account as from the date of the dissolution.

30. (1) A person who is a minor according to the law to which he is subject may not be a partner in a firm, but, with the consent of all the partners for the time being, he may be admitted to the benefits of partnership.

(2) Such minor has a right to such share of the property and of the profits of the firm as may be agreed upon, and he may have access to and inspect and copy any of the accounts of the firm.

(3) Such minor's share is liable for the acts of the firm, but the minor is not personally liable for any such act.

(4) Such minor may not sue the partners for an account or payment of his share of the property or profits of the firm, save when severing his connection with the firm, and in such case the amount of his share shall be determined by a valuation made as far as possible in accordance with the rules contained in section 48:

Provided that all the partners acting together or any partner entitled to dissolve the firm upon notice to other partners may elect in such a suit to dissolve the firm, and thereupon the Court shall proceed with the suit as one for dissolution and for settling accounts between the partners, and the amount of the share of the minor shall be determined along with the shares of the partners.

(5) At any time within six months of his attaining majority, or of his obtaining knowledge that he had been admitted to the benefits of partnership, whichever date is later, such person may give public notice that he has elected to become or that he has elected not to become a partner in the firm, and such notice shall determine his position as regards the firm :

Provided that if he fails to give such notice, he shall become a partner in the firm on the expiry of the said six months.

(6) Where any person has been admitted as a minor to the benefits of partnership in a firm, the burden of proving the fact that such person had no knowledge of such admission until a particular date after the expiry of six months of his attaining majority shall lie on the persons asserting that fact.

(7) Where such person becomes a partner,—

(a) his rights and liabilities as a minor continue up to the date on which he becomes a partner, but he also becomes personally liable to third parties for all acts of the firm done since he was admitted to the benefits of partnership, and

(b) his share in the property and profits of the firm shall be the share to which he was entitled as a minor.

(8) Where such person elects not to become a partner,—

(a) his rights and liabilities shall continue to be those of a minor under this section up to the date on which he gives public notice,

- (b) his share shall not be liable for any acts of the firm done after the date of the notice, and
  - (c) he shall be entitled to sue the partners for his share of the property and profits in accordance with sub-section (4).
- '.' (9) Nothing in sub-sections (7) and (8) shall affect the provisions of section 28.

## CHAPTER V

### Incoming and outgoing partners

31. (1) Subject to contract between the partners and to the provisions of section 30, no person shall be introduced as a partner into a firm, without the consent of all the existing partners.

Introduction of a partner. (2) Subject to the provisions of section 30, a person who is introduced as a partner into a firm does not thereby become liable for any act of the firm done before he became a partner.

32. (1) A partner may retire--

Retirement of a partner. (a) with the consent of all the other partners,

(b) in accordance with an express agreement by the partners,  
or

(c) where the partnership is at will, by giving notice in writing to all the other partners of his intention to retire.

(2) A retiring partner may be discharged from any liability to any third party for acts of the firm done before his retirement by an agreement made by him with such third party and the partners of the reconstituted firm, and such agreement may be implied by a course of dealing between such third party and the reconstituted firm after he had knowledge of the retirement.

(3) Notwithstanding the retirement of a partner from a firm, he and the partners continue to be liable as partners to third parties for any act done by any of them which would have been an act of the firm if done before the retirement, until public notice is given of the retirement.

Provided that a retired partner is not liable to any third party who deals with the firm without knowing that he was a partner.

(4) Notices under sub-section (3) may be given by the retired partner or by any partner of the reconstituted firm.

33. (1) A partner may not be expelled from a firm by any majority of the partners, save in the exercise of the Expulsion of a partner in good faith of powers conferred by contract between the partners.

(2) The provision of sub-sections (2), (3) and (4) of section 32 shall apply to an expelled partner as if he were a retired partner.

34. (1) Where a partner in a firm is adjudicated an insolvent Insolvency of a partner he ceases to be a partner on the date on which the order of adjudication is made, whether or no, the firm is thereby dissolved.

(2) Where under a contract between the partners, the firm is not dissolved by the adjudication of a partner as an insolvent the estate of a partner so adjudicated is not liable for any act of the firm and the firm is not liable for any act of the insolvent, done after the date on which the order of adjudication is made.

35. Where under a contract between the partners the firm is not dissolved by the death of a partner, the estate of a deceased partner is not liable for any act of the firm done after his death.

36. (1) An outgoing partner may carry on a business Rights of outgoing partner to competing with that of the firm and he may carry on competing business. to contrary he may not : -

(a) use the firm name,

(b) represent himself as carrying on the business of the firm, or

(c) solicit the custom of persons who were dealing with the firm before he ceased to be a partner.

(2) A partner may make an agreement with his partners that on ceasing to be a partner he will not carry on any business similar to that of the firm within a specified period or within specified local limits ; and, notwithstanding anything contained in section 27 of the Indian Contract Act, 1872, such agreement shall be valid if the restrictions imposed are reasonable.

**Right of outgoing partner in certain cases to share subsequent profits.** 37. Where any member of a firm has died or otherwise ceased to be a partner, and the surviving or continuing partners carry on the business of the firm with the property of the firm without any final settlement of accounts as between them and the outgoing partner or his estate, then, in the absence of a contract to the contrary, the outgoing partner or his estate is entitled at the option of himself or his representatives to such share of the profits made since he ceased to be a partner as may be attributable to the use of his share of the property of the firm or to interest at the rate of six per cent. per annum on the amount of his share in the property of the firm ;

Provided, that where by contract between the partners in option is given to surviving or continuing partners to purchase the interest of a deceased or outgoing partner, and that option is duly exercised, the estate of the deceased partner or the outgoing partner or his estate, as the case may be, is not entitled to any further or other share of profits ; but if any partner assuming to act in exercise of the option does not in all material respects comply with the terms thereof, he is liable to account under the foregoing provisions of this section.

38. A continuing guarantee given to a firm, or to a third party in respect of transactions of a firm, is, in the absence of agreement to the contrary, revoked as to future transactions from the date of any change in the constitution of the firm.

## CHAPTER VI

### Dissolution of a Firm

**Dissolution of a firm.** 39. The dissolution of a partnership between all the partners of a firm is called the "dissolution of the firm".

**Dissolution by agreement.** 40. A firm may be dissolved with the consent of all the partners or in accordance with a contract between the partners.

41. A firm is dissolved :—

**Compulsory dissolution.** (a) by the adjudication of all the partners or of all the partners but one as insolvent, or

(b) by the happening of any event which makes it unlawful for the business of the firm to be carried on or for the partners to carry it on in partnership :

Provided that, where more than one separate adventure or undertaking is carried on by the firm, the illegality of one or more shall not of itself cause the dissolution of the firm in respect of its lawful adventures and undertakings.

42. Subject to contract between the partners a firm is dissolved :—

(a) if constituted for a fixed term, by the expiry of that [redacted].

- (b) if constituted to carry on more adventures or undertakings, by the [redacted] of [redacted] ;
- (c) by the death of a partner [redacted].
- (d) by the adjudication of a partner [redacted].

43. (1) Where the partnership is at will [redacted] be dissolved by any partner giving notice to all the other partners of his [redacted] dissolve the firm.

(2) The firm is dissolved as from the date mentioned in the notice as the date of dissolution or, if no date is so mentioned as from the date of the communication of the notice.

44. At the suit of a partner, the Court may dissolve a firm on any of the following grounds, namely :—

- (a) that a partner has become of unsound mind, in which case the suit may be brought as well by the next friend of the partner who has become of unsound mind as by any other partner ;
- (b) that a partner, other than the partner suing, has become in any way permanently incapable of performing his duties as partner ;
- (c) that a partner, other than the partner suing, is guilty of conduct which is likely to affect prejudicially the carrying on of the business, regard being had to the nature of the business ;
- (d) that a partner, other than the partner suing, wilfully or persistently commits breach of agreements relating to the management of the affairs of the firm or the conduct of its business, or otherwise so conducts

himself in matters relating to the business that it is not reasonably practicable for the other partners to carry on the business in partnership with him,

- (e) that a partner, other than the partner suing, has in any way transferred the whole of his interest in the firm to a third party, or has allowed his share to be charged under the provisions of rule 49 of Order XXI of the First Schedule to the Code of Civil Procedure, 1908, or has allowed it to be sold in the recovery of arrears of land-revenue or of an ~~any~~ recoverable as arrears of land-revenue due by the partner;
- (f) that the business of the firm cannot be carried on satisfactorily at a ~~any~~
- (g) ~~any~~ which renders it just and equitable that the firm should be dissolved.

Notwithstanding the dissolution of a firm, the partners continue to be liable as such to third persons for any act done by any of them which would have been an act of the firm if done before the dissolution, until public notice is given of the dissolution.

Provided that the estate of a partner who dies, or who is adjudicated an insolvent, or of a partner who, not having been known to the person dealing with the firm to be a partner, ceases from the firm, is not liable under this section for acts done after the date on which he ceases to be a partner.

(2) Notices under subsection (1) may be given by my partner.

**46. On the dissolution of a firm every partner or his representative is entitled, as against all the other partners or their representatives, to have the property of the firm applied in payment of the debts and liabilities of the firm, and to have the surplus distributed among the partners or their representatives according to their rights.**

**47. After the dissolution of a firm the authority of each partner to bind the firm, and the other mutual rights and obligations of the partners continue notwithstanding the dissolution, so far as may be necessary to wind up the affairs of the firm and**

to complete transactions begun but unfinished at the time of the dissolution, but not otherwise :

Provided that the firm is in no case bound by the acts of a partner who has been adjudicated insolvent ; but this proviso does not affect the liability of any person who has after the adjudication represented himself or knowingly permitted himself to be represented as a partner of the insolvent.

48. In settling the accounts of a firm after dissolution, the Mode of settle- following rules shall, subject to agreement by the ment of accounts partners, be observed :—

(a) Losses, including deficiencies of capital, shall be paid first out of profits, next out of capital, and, lastly, if necessary, by the partners individually in the proportions in which they were entitled to share profits.

(b) The assets of the firm, including any sums contributed by the partners to make up deficiencies of capital, shall be applied in the following manner and order :—

- (i) in paying the debts of the firm to third parties ;
- (ii) in paying to each partner rateably what is due to him from the firm for advances as distinguished from capital ;
- (iii) in paying to each partner rateably what is due to him on account of capital ; and
- (iv) the residue, if any, shall be divided among the partners in the proportions in which they were entitled to share profits.

49. Where there are joint debts from the firm, and also separate debts due from any partner, the property debts and of the firm shall be applied in the first instance separate debts. in payment of the debts of the firm, and, if there is any surplus, then the share of each partner shall be applied in payment of his separate debts or paid to him. The separate property of any partner shall be applied first in the payment of his separate debts, and the surplus (if any) in the payment of the debts of the firm.

50. Subject to contract between the partners, the provisions

Personal profits of clause (s) of section 16 shall apply to transactions by any surviving partner or by the representatives of a deceased partner, undertaken after the firm is dissolved on account of the death of a partner and before its affairs have been completely wound up :

Provided that where any partner or his representative has bought the goodwill of the firm, nothing in this section shall affect his right to use the firm name.

51. Where a partner has paid a premium on entering into partnership for a fixed term, and the firm is dissolved before the expiration of that term otherwise than by the death of a partner, he shall be entitled to repayment of the premium or of such part thereof as may be reasonable, regard being had to the terms upon which he became a partner and to the length of time during which he was a partner, unless—

(a) the dissolution is mainly due to his own misconduct,  
or

(b) the dissolution is in pursuance of an agreement containing no provision for the return of the premium or any part of it.

52. Where a contract creating partnership is rescinded on the ground of the fraud or misrepresentation of any of the parties thereto, the party entitled to rescind is, without prejudice to any other right, entitled—

(a) to a lien on, or a right of retention of, the surplus or the assets of the firm remaining after the debts of the firm have been paid, for any sum paid by him for the purchase of a share in the firm and for any capital contributed by him :

(b) to rank as a creditor of the firm in respect of any payment made by him towards the debts of the firm; and

(c) to be indemnified by the partner or partner guilty of the fraud or misrepresentation against all the debts of the firm.

**53.** After a firm is dissolved, every partner or his representative may, in the absence of a contract between the partners to the contrary, restrain any other partner or his representative from carrying on a similar business in the firm name or from using any of the property of the firm for his own benefit, until the affairs of the firm have been completely wound up:

Right to restrain from use of firm name or firm property. Provided that where any partner or his representative has bought the goodwill of the firm, nothing in this section shall affect his right to use the firm name.

**54.** Partners may, upon or in anticipation of the dissolution of the firm, make an agreement that some or all of them will not carry on a business similar to that of the firm Agreements in restraint of trade. within a specified period or within specified local limits; and notwithstanding anything contained in section 27 of the Indian Contract Act, 1872, such agreement shall be valid if the restrictions imposed are reasonable.

**55.** (1) In settling the accounts of a firm after dissolution, the goodwill shall, subject to contract between Sale of goodwill after dissolution. the partners, be included in the assets, and it may be sold either separately or along other property of the firm.

(2) Where the goodwill of a firm is sold after dissolution, Rights of buyer and seller of goodwill. a partner may carry on a business competing with that of the buyer and he may advertise such business, but, subject to agreement between him and the buyer, he may not—

- (a) use the firm name,
- (b) represent himself as carrying on the business of the firm, or
- (c) solicit the custom of persons who were dealing with the firm before its dissolution.

(3) Any partner may, upon the sale of the goodwill of a firm, make an agreement with the buyer that such partner will not Agreements in restraint of trade. carry on any business similar to that of the firm within a specified period or within specified local limits, and, notwithstanding anything contained in section 27 of the Indian Contract Act, 1872, such agreement shall be valid if the restrictions imposed are reasonable.

## CHAPTER VII

### Registration of Firms

56. The Governor-General in Council may, by notification in the Gazette of India, direct that the provisions of this Chapter shall not apply to any province or to any part thereof in the notification.

57. (1) The Local Government may appoint Registrars of Firms for the purposes of this Act, and may fix the areas within which they shall exercise their powers and perform their duties.

(2) Every Registrar shall be deemed to be a public servant within the meaning of section 21 of the Indian Penal Code.

58. (1) The registration of a firm may be effected at any time by sending by post or delivering to the Registrar of the area in which any place of business of the firm is situated or proposed to be situated, a statement in the prescribed form and accompanied by the prescribed fee, stating—

- (a) the firm name,
- (b) the place or principal place of business of the firm,
- (c) the names of any other places where the firm carries on business,
- (d) the date when each partner joined the firm,
- (e) the names in full and permanent addresses of the partners, and
- (f) the duration of the firm.

The statement shall be signed by all the partners, or by their agents specially authorised in this behalf.

(2) Each person signing the statement shall also verify it in the manner prescribed.

(3) A firm name shall not contain any of the following words, namely —

"Crown," "Emperor," "Empress," "Empire", "Imperial", "King", "Queen", "Royal", or words expressing or implying the sanction, approval or patronage of the Crown or the Government of India or a Local Govern-

ment, except when the Governor-General in Council signifies his consent to the use of such words as part of the firm name by order in writing under the hand of one of the Secretaries of the Government of India.

59. When the Registrar is satisfied that the provisions of section 58 have been duly complied with, he shall record an entry of the statement in a register called the Register of Firms, and shall file the statement.

Recording of alterations in firm name and principal place of business.

60. (1) When an alteration is made in the firm name or in the location of the principal place of business of a registered firm, a statement may be sent to the Registrar accompanied by the prescribed fee, specifying the alteration, and signed and verified in the manner required under section 58.

(2) When the Registrar is satisfied that the provisions of sub-section (1) have been duly complied with, he shall amend the entry relating to the firm in the Register of Firms in accordance with the statement, and shall file it along with the statement relating to the firm filed under section 59.

Nothing of closing and opening of branches.

61. When a registered firm discontinues business at any place or begins to carry on business at any place, such place not being its principal place of business, any partner or agent of the firm may send intimation thereof to the Registrar, who shall make a note of such intimation in the entry relating to the firm in the Register of Firms, and shall file the intimation along with the statement relating to the firm filed under section 59.

Nothing of changes in names and address of partners.

62. When any partner in a registered firm alters his name or permanent address, an intimation of the alteration may be sent by any partner or agent of the firm to the Registrar, who shall deal with it in the manner provided in section 61.

Recording of changes in and dissolution of a firm.

63. (1) When a change occurs in the constitution of a registered firm any incoming, continuing or outgoing partner, and when a registered firm is dissolved any person who was a partner immediately before the dissolution, or the agent of any such partner or person specially authorised in this behalf, may give notice to the Registrar of such change or dissolution, specify-

ing the date thereof ; and the Registrar shall make a record of the notice in the entry relating to the firm in the Register of Firms, and shall file the notice along with the statement relating to the firm filed under section 59.

(2) When a minor who has been admitted to the benefits of partnership in a firm attains majority and elects to become or not to become a partner, and the firm is then a registered firm, he or his agent specially authorised in this behalf, may give notice to the Registrar that he has or has not become a partner, and the Registrar shall deal with the notice in the manner provided in subsection (1).

64. (1) The Registrar shall have power at all times to rectify any mistake in order to bring the entry in the Register of Firms relating to any firm in conformity with the documents relating to that firm filed under this Chapter.

(2) On application made by all the parties who have signed any document relating to a firm filed under this Chapter, the Registrar may rectify any mistake in such document or in the record or note thereof made in the Register of Firms.

65. A Court deciding any matter relating to a registered firm may direct that the Registrar shall make any amendment in the entry in the Register of Firms relating to such firm which is consequential upon its decision ; and the Registrar shall amend the entry accordingly.

66. (1) The Register of Firms shall be open to inspection by any person on payment of such fee as may be prescribed.

(2) All statements, notices and intimations filed under this Chapter shall be open to inspection, subject to such conditions and on payment of such fee as may be prescribed.

67. The Registrar shall on application furnish to any person, any payment of such fee as may be prescribed, a copy certified under his hand, of any entry or portion thereof in the Register of Firms.

68. (1) Any statement, intimation or notice recorded or noted in the Register of Firms shall, as against any person by whom or on whose behalf such

statement, intimation or notice was signed, be conclusive proof of any fact therein stated.

(2) A certified copy of an entry relating to a firm in the Register of Firms may be produced in proof of the fact of the registration of such firm, and of the contents of any statement, intimation or notice recorded or noted therein.

69. (1) No suit to enforce a right arising from a contract or conferred by this Act shall be instituted in any Court by or on behalf of any person suing as a partner in a firm against the firm or any person alleged to be or to have been a partner in the firm unless the firm is registered and the person suing is or has been shown in the Register of Firms as a partner in the firm.

(2) No suit to enforce a right arising from a contract shall be instituted in any Court by or on behalf of a firm against any third party unless the firm is registered and the persons suing are or have been shown in the Register of Firms as partners in the firm.

(3) The provisions of sub-sections (1) and (2) shall apply also to a claim of set-off or other proceeding to enforce a right arising from a contract, but shall not affect—

(a) the enforcement of any right to sue for the dissolution of a firm or for accounts of a dissolved firm, or any right or power to realise the property of a dissolved firm, or

(b) the powers of an official assignee, receiver or Court under the Presidency-towns Insolvency Act, 1909, or the Provincial Insolvency Act, 1920, to realise the property of an insolvent partner.

(4) This section shall not apply—

(a) to firms or to partners in firms which have no place of business in British India, or whose places of business in British India are situated in areas to which, by notification under section 55, this Chapter does not apply, or

(b) to any suit or claim of set-off not exceeding one hundred rupees in value which in the Presidency-towns, is not of a kind specified in section 19 of the Presidency

Small Cause Courts Act, 1882 or outside the Presidency-towns, is not of a kind specified in the Second Schedule to the Provincial Small Cause Courts Act, 1887 or to any proceeding in execution or other proceeding incidental to or arising from any such suit or claim.

70. Any person who signs any statement, amending statement, notice or intimation under this Chapter containing any particular which he knows to be false or does not believe to be true, or containing particulars which he knows Penalty for furnishing to be incomplete or does not believe to be containing false particulars, shall be punishable with imprisonment which may extend to three months or with fine, or with both.

71. (1) The Governor-General in Council may make rules prescribing the fees which shall accompany documents sent to the Registrar of Firms, or which shall be payable Power to make rules. for the inspection of documents in the custody of the Registrar of Firms, or for copies from the Register of Firms :

Provided that such fees shall not exceed the maximum fees, specified in Schedule I.

- (2) The Local Government may make rules—
  - (a) prescribing the form of statement submitted under section 58, and of the verification thereof ;
  - (b) requiring statements, intimations and notices under sections 60, 61, 62 and 63 to be in prescribed form, and prescribing the form thereof ;
  - (c) prescribing the form of the Register of Firms, and the mode in which entries relating to firms are to be made therein, and the mode in which such entries are to be amended or notes made therein ;
  - (d) regulating the procedure of the Registrar when disputes arise ;
  - (e) regulating the filing of documents received by the Registrar ;
  - (f) prescribing conditions for the inspection of original documents ;
  - (g) regulating the grant of copies ;
  - (h) regulating the elimination of registers and documents ;

- (i) providing for the maintenance and form of an Index to the Register of Firms ; and
  - (j) generally, to carry out the purposes of this Chapter.
- (3) All rules made under this section shall be subject to the condition of previous publication.

## CHAPTER VIII

### **Supplemental**

72. A public notice under this Act is given—
- (a) where it relates to the retirement or expulsion of a partner from a registered firm or to the dissolution of a registered firm, or to the election to become or not to become a partner in a registered firm by a person attaining majority who was admitted as a minor to the benefits of partnership, by notice to the Registrar of Firms under section 63, and by publication in the local official Gazette and in at least one vernacular newspaper circulating in the district where the firm to which it relates has its place or principal place of business, and
  - (b) in any other case, by publication in the local official Gazette and in at least one vernacular newspaper circulating in the district where the firm to which it relates has its place or principal place of business.
73. The enactments mentioned in Schedule II are hereby repealed to the extent specified in the fourth column thereof.
74. Nothing in this Act or any repeal effected thereby shall affect or be deemed to affect—
- (a) any right, title, interest, obligation or liability already acquired, accrued or incurred before the commencement of this Act, or
  - (b) any right, title, interest, obligation or liability, or anything done or suffered before the commencement of this Act, or
  - (c) anything done or suffered before the commencement of this Act, or

- (d) any enactment relating to partnership not expressly repealed by this Act, or
- (e) any rule of insolvency relating to partnership, or
- (f) any rule of law not inconsistent with this Act.

### SCHEDULE I

#### Maximum Fees

[See sub-section (1) of section 71.]

Document or act in respect of which the fee is payable.	Maximum fee.
Statement under section 58 . . .	Three rupees.
Statement under section 60 . . .	One rupee.
Intimation under section 61 . . .	One rupee.
Intimation under section 62 . . .	One rupee.
Notice under section 63 . . .	One rupee.
Application under section 64 . . .	One rupee.
Inspection of the Register of Firms under sub-section (1) of section 66.	Eight annas for inspecting one volume of the Register.
Inspection of documents relating to a firm under sub-section (2) of section 66.	Eight annas for the inspection of all documents relating to one firm.
Copies from the Register of Firms.	Four annas for each hundred words or part thereof.

### SCHEDULE II

#### Enactments Repealed

(See section 73.)

Year. 1	No. 2	Short title. 3	Extent of repeal. 4
1872	IX	The Indian Contract Act, 1872.	Exceptions 2 & 3 to section 27. The whole of Chapter XI.
1920	Burma Act VIII.	The Burma Registration of Business Names Act, 1920.	The whole.

**The Negotiable Instruments  
Act, 1887.  
(No. XXVI of 1881)**

An Act to define and amend the law relating to Promissory Notes, Bills of Exchange and Cheques.  
[ As modified up to the 1st May, 1935.]

Preamble. Whereas it is expedient to define and amend the law relating to promissory notes, bills of exchange and cheques; It is hereby enacted as follows :—

**CHAPTER I  
Preliminary**

1. This Act may be called the Negotiable Instruments Short title. Act, 1881 :

It extends to the whole of British India ; but nothing herein contained affects the Indian Paper Currency Act, 1871, section 21, or affects any local usage relating to any instrument in an oriental language ; Provided that such usages may be excluded by any words in the body of the instrument which indicate an intention that the legal relations of the parties thereto shall be governed by this Act ; and it shall come into force on the first day of March, 1882.

2. [ *Repeal of enactments.* ] Repealed by the Repealing and Amending Act, 1891 (XII of 1891).

3. In this Act—

Interpretation clause.

“banker” includes also persons or corporation or company “Banker.” acting as bankers ; and

“notary public” includes also any person appointed by the Local Government to perform the functions of a “Notary public.” notary public under this Act.

## CHAPTER II

### Of Notes, Bills and Cheques

4. A "promissory note" is an instrument in writing (not being a bank-note or a currency-note) containing "Promissory note." an unconditional undertaking, signed by the maker, to pay a certain sum of money only to, or to the order of, a certain person, or to the bearer of the instrument.

#### *Illustrations*

A signs instruments in the following terms :

- (a) "I promise to pay B or order Rs. 500."
- (b) "I acknowledge myself to be indebted to B in Rs. 1,000, to be paid on demand, for value received."
- (c) "Mr. B. I. O. U. Rs. 1,000."
- (d) "I promise to pay B Rs. 500 and all other sums which shall be due to him."
- (e) "I promise to pay B Rs. 500, first deducting therewith any money which he may owe me."
- (f) "I promise to pay B Rs. 500 seven days after my marriage with C."
- (g) "I promise to pay B Rs. 500 on D's death, provided D leaves me enough to pay that sum."
- (h) "I promise to pay B Rs. 500 and to deliver to him my black horse on 1st January next."

The instruments respectively marked (a) and (b) are promissory notes. The instruments respectively marked (c), (d), (e), (f), (g) and (h) are not promissory notes.

5. A "bill of exchange" is an instrument in writing containing "Bill of exchange." an unconditional order, signed by the maker, directing a certain person to pay a certain sum of money only to or to the order of, a certain person or to the bearer of the instrument.

A promise or order to pay is not "conditional," within the meaning of this section and section 4, by reason of the time for

payment of the amount or any instalment thereof being expressed to be on the lapse of a certain period after the occurrence of a specified event which, according to the ordinary expectation of mankind, is certain to happen, although the time of its happening may be uncertain. The sum payable may be "certain," within the meaning of this section and section 4, although it includes future interest or is payable at an indicated rate of exchange, or is according to the course of exchange, and although the instrument provides that, on default of payment of an instalment, the balance unpaid shall become due.

The person to whom it is clear that the direction is given or that payment is to be made may be a "certain person," within the meaning of this section and section 4, although he is misnamed or designated by description only.

6. A "cheque" is a bill of exchange drawn on a specified banker and not expressed to be payable otherwise than "Cheque." "on demand."

7.. The maker of a bill of exchange or cheque is called the "Drawer." "drawer," the person thereby directed to pay is "Drawee." called the "drawee."

When in the bill or in any indorsement thereon the name of any person is given in addition to the drawee to "Drawee in case be restored to in case of need, such person is called of need." a "drawee in case of need."

After the drawee of a bill has signed his assent upon the bill, "Acceptor." or, if there are more parts thereof than one, upon one of such parts, and delivered the same or given notice of such signing to the holder or to some person on his behalf he is called the "acceptor."

When a bill of exchange has been noted or protested for non-acceptance or for better security and any person "Acceptor for honour." accepts it *supra protest* for honour of the drawer or for any one of the indorsers, such person is called an "acceptor for honour."

The person named in the instrument, to whom or to whose order the money is by the instrument directed to "Payee." be paid, is called the "payee."

8. The "holder" of a promissory note, bill of exchange or cheque means any person entitled in his own "Holder" name to the possession thereof and to receive or recover the amount due thereon from the parties thereto.

Where the note, bill or cheque is lost or destroyed, its holder is the person so entitled at the time of such loss or destruction.

9. "Holder in due course" means any person who for consideration became the possessor of a promissory note, bill of exchange or cheque if payable to bearer,

or the payee or indorsee thereof, if payable to order before the amount mentioned in it became payable, and without having sufficient cause to believe that any defect existed in the title of the person from whom he derived his title.

10. "Payment in due course" means payment in accordance with the apparent tenor of the instrument in good faith and without negligence to any person in possession "Payment in due thereof under circumstances which do not afford course." a reasonable ground for believing that he is not entitled to receive payment of the amount therein mentioned.

11. A promissory note, bill of exchange or cheque drawn or "Inland instru- made in British India, and made payable in, or ment" drawn upon any person resident in British India, shall be deemed to be an inland instrument.

12. Any such instrument not so drawn, made or made payable "Foreign instru- shall be deemed to be a foreign instrument. ment."

13. (1) A "negotiable instrument" means a promissory note, "Negotiable bill of exchange or cheque payable either to order instrument." or to bearer.

*Explanation (i)*—A promissory note, bill of exchange or cheque is payable to order which is expressed to be so payable or which is expressed to be payable to a particular person, and does not contain words prohibiting transfer or indicating an intention that it shall not be transferable.

*Explanation (ii)* A promissory note, bill of exchange or cheque is payable to bearer which is expressed to be so payable or on which the only or last indorsement is an indorsement in blank.

*Explanation (iii)*—Where a promissory note, bill of exchange or cheque, either originally or by indorsement, is expressed to be payable to the order of a specified person, and not to him or his order, it is nevertheless payable to him or his order at his option.

(2) A negotiable instrument may be made payable to two or more payees jointly, or it may be made payable in the alternative to one of two, or one or some of several payees.

14. When a promissory note, bill of exchange or cheque is transferred to any person, so as to constitute that Negotiation. person the holder thereof, the instrument is said to be negotiated.

15. When the maker or holder of a negotiable instrument signs the same, otherwise than as such maker, for the purpose of Indorsement. negotiation, on the back or face thereof or on a slip of paper annexed thereto, or so signs for the same purpose a stamped paper intended to be completed as a negotiable instrument, he is said to indorse the same, and is called the "indorser."

16. (1) If the indorser signs his name only, the indorsement Indorsement "in blank" and "in full." is said to be "in blank", and if he adds a direction to pay the amount mentioned in the instrument to, or to the order of, a specified person, the "Indorsee." indorsement is said to be "in full"; and the person so specified is called the "indorsee" of the instrument.

(2) The provisions of this Act relating to a payee shall apply with the necessary modifications to a indorsee.

17. Where an instrument may be construed either as a Ambiguous instruments. promissory note or bill of exchange, the holder may, at his election treat it as either, and the instrument shall be thenceforward treated accordingly.

18. If the amount undertaken or ordered to be paid is stated Where amount is stated differently in figures and in words, the amount stated in words shall be the amount undertaken figures and words. or ordered to be paid.

19. A promissory note or bill of exchange, in which no time Instruments pay. for payment is specified, and a cheque, are payable on demand. able, on demand.

20. Where one person signs and delivers to another a paper stamped in accordance with the law relating to negotiable instruments then in force in British India, and either wholly blank or having written thereon an incomplete negotiable instrument, he thereby gives *prima facie* authority to the holder thereof to make or complete, as the case may be, upon it a negotiable instrument, for any amount specified therein and not exceeding the amount covered by the stamp. The person so signing shall be liable upon such instrument, in the capacity in which he signed the same, to any holder in due course for such amount : Provided that no person other than a holder in due course shall recover from the person delivering the instrument anything in excess of the amount intended by him to be paid thereunder.

21. In a promissory note or bill of exchange the expressions "At sight." "On presentation." "at sight" and "on presentment" mean on demand. The expression, "after sight" means, in a promissory note, after presentment for sight, and, in a bill of exchange, after acceptance, or noting for non-acceptance, or protest for non-acceptance.

22. The maturity of a promissory note or bill of exchange is "Maturity." the date at which it falls due.

Every promissory note or bill of exchange which is not expressed to be payable on demand, at sight or on Days of grace. presentment is at maturity on the third day after the day on which it is expressed to be payable.

23. In calculating the date at which a promissory note or bill of exchange, made payable a stated number of months after date or after sight, or after a certain event, is at maturity, the period stated shall be held to terminate on the day of the month which or sight.

corresponds with the day on which the instrument is dated, or presented for acceptance or sight, or noted for non-acceptance, or protested for non-acceptance, or the event happens, or, where the instrument is a bill of exchange made payable a stated number of months after sight and has been accepted for honour, with the day on which it was so accepted. If the month in which the period would terminate has no corresponding day, the period shall be held to terminate on the last day of such month.

*Illustrations*

(a) A negotiable instrument, dated 29th January, 1878, is made payable at one month after date. The instrument is at maturity on the third day after the 28th February, 1878.

(b) A negotiable instrument dated 30th August, 1878, is made payable three months after date. The instrument is at maturity on the 3rd December, 1878.

(c) A promissory note or bill of exchange, dated 31st August, 1878, is made payable three months after date. The instrument is at maturity on the 3rd December, 1878.

**24. In calculating the date at which a promissory note or bill of exchange made payable a certain number of days after date or after sight or after a certain event is at maturity, the day of the date, or of presentment for acceptance or sight, or of protest**

**Calculating maturity of bill or note payable so many days after date or sight.**

for non-acceptance, or on which the event happens, shall be excluded.

**25. When the day on which a promissory note or bill of exchange is at maturity is a public holiday, the instrument shall be deemed to be due on the next preceding business day.**

**When day of maturity is a holiday.**

*Explanation* :—The expression "public holiday" includes Sundays, New Year's day, Christmas day : if, either of such days falls on a Sunday, the next following Monday : Good Friday ; and any other day declared by the Local Government, by notification in the official Gazette, to be a public holiday.

**CHAPTER III****Parties to Notes, Bills and Cheques**

**26. Every person capable of contracting, according to the law to which he is subject, may bind himself and be bound by the making, drawing, acceptance, indorsement, delivery and negotiation of a promissory note, bill of exchange or cheque.**

**Capacity to make, etc., promissory notes, etc.**

A minor may draw, indorse, deliver and negotiate such instrument so as to bind all parties except himself.

Nothing herein contained shall be deemed to empower a corporation to make, indorse or accept such instruments except in cases in which, under the law for the time being in force, they are so empowered.

27. Every person capable of binding himself or of being bound, as mentioned in section 26, may so bind himself or be bound by a duly authorized agent acting in his name.

A general authority to transact business and to receive and discharge debts does not confer upon an agent the power of accepting or indorsing bills of exchange so as to bind his principal.

An authority to draw bills of exchange does not of itself import an authority to indorse.

28. An agent who signs his name to a promissory note, bill of exchange or cheque without indicating thereon that he signs as agent, or that he does not intend thereby to incur personal liability of agent responsibility, is liable personally on the instrument, except to those who induced him to sign upon the belief that the principal only would be held liable.

29. A legal representative of a deceased person who signs his name to a promissory note, bill of exchange or cheque is liable personally thereon unless he expressly limits his liability to the extent of the assets received by him as such.

30. The drawer of a bill of exchange or cheque is bound, in case of dishonour by the drawee or acceptor thereof, to compensate the holder, provided due notice of dishonour has been given to, or received by, the drawer as hereinafter provided.

31. The drawee of a cheque having sufficient funds of the drawer in his hands, properly applicable to the payment of such cheque must pay the cheque when duly required so to do, and, in default of such payment, must compensate the drawee for any loss or damage caused by such default.

**32.** In the absence of a contract to the contrary the maker of a promissory note and the acceptor before maturity of a bill of exchange are bound to pay the amount thereof at maturity according to the apparent tenor of the note or acceptance respectively, and the acceptor of a bill of exchange at or after maturity is bound to pay the amount thereof to the holder on demand.

In default of such payment as aforesaid, such maker or acceptor is bound to compensate any party to the note or bill for any loss or damage sustained by him and caused by such default.

**33.** No person except the drawee of a bill of exchange or all Only drawee can be acceptor except in need or honour. or some of several drawees, or a person named therein as a drawee in case of need, or an acceptor for honour, can bind himself by an acceptance.

**34.** Where there are several drawees of a bill of exchange Acceptance by several drawees who are not partners, each of them can accept it for himself, but none of them can accept it for another without his authority.

**35.** In the absence of a contract to the contrary, whoever Liability of indorser and delivers a negotiable instrument before maturity, without, in such indorsement, expressly excluding or making conditional his own liability, is bound thereby to every subsequent holder, in case of dishonour by the drawee, acceptor or maker to compensate such holder for any loss or damage caused to him by such dishonour, provided due notice of dishonour has been given to or received by, such indorser as hereinafter provided.

Every indorser after dishonour is liable as upon an instrument payable on demand.

**36.** Every prior party to a negotiable instrument is liable Liability of prior parties to holder in due course until the instrument is duly satisfied.

**37.** The maker of a promissory note or cheque, the drawer of a bill of exchange until acceptance, and the acceptor are, in the absence of a contract to the contrary, respectively liable thereon as principal debtors, and the other parties thereto are liable thereon as sureties for the maker, drawer or acceptor, as the case may be.

38. As between the parties so liable as sureties, each prior party is in the absence of a contract to the contrary, also liable thereon as a principal debtor in respect of each subsequent party.

*Illustration*

A draws a bill payable to his own order on B, who accepts. A afterwards indorses the bill to C, C to D and D to E. As between E and B, B is the principal debtor, and A, C and D are his sureties. As between E and A, A is the principal debtor, and C and D are his sureties. As between E and C, C is the principal debtor and D is his surety.

39. When the holder of an accepted bill of exchange enters into any contract with the acceptor which, under <sup>Suretyship.</sup> section 134 or 135 of the Indian Contract Act, IX of 1872, 1872, would discharge the other parties, the holder may expressly reserve his right to charge the other parties, and in such case they are not discharged.

40. When the holder of a negotiable instrument, without the consent of the indorser, destroys the indorser's remedy against a prior party, the indorser is discharged from liability to the holder to the same extent as if the instrument had been paid at maturity.

*Illustration*

A is the holder of a bill of exchange made payable to the order of B, which contains the following indorsements in blank :—

First indorsement, "B".

Second indorsement, "Peter Williams."

Third indorsement, "Wright & Co."

Fourth indorsement, "John Rozario."

This bill A puts in suit against John Rozario and strikes out, without John Rozario's consent, the indorsements by Peter Williams and Wright & Co. A is not entitled to recover anything from John Rozario.

41. An acceptor of a bill of exchange already indorsed is not relieved from liability by reason that such indorsement is forged, if he knew or had reason to believe the indorsement to be forged when he accepted the bill.

Acceptor bound although indorsement forged.

Acceptance of bill drawn in fictitious name. 42. An acceptor of a bill of exchange drawn in a fictitious name and payable to the drawer's order is not, by reason that such name is fictitious, relieved from liability to any holder in due course claiming under an indorsement by the same hand as the drawer's signature, and purporting to be made by the drawer.

Negotiable instrument made, etc. without consideration. 43. A negotiable instrument made, drawn, accepted, indorsed or transferred without consideration, or for a consideration which fails, creates no obligation of payment between the parties to the transaction. But if any such party has transferred the instrument with or without indorsement to a holder for consideration, such holder, and every subsequent holder deriving title from him, may recover the amount due on such instrument from the transferor for consideration or any prior party thereto.

*Exception I.*—No party for whose accommodation a negotiable instrument has been made, drawn, accepted or indorsed can, if he has paid the amount thereof, recover thereon such amount from any person who became a party to such instrument for his accommodation.

*Exception II.*—No party to the instrument who has induced any other party to make, draw, accept, indorse or transfer the same to him for a consideration which he has failed to pay or perform in full shall recover thereon an amount exceeding the consideration (if any) which he has actually paid or performed.

Partial absence or failure of money-consideration. 44. When the consideration for which a person signed a promissory note, bill of exchange or cheque consisted of money, and was originally absent in part or has subsequently failed in part, the sum which a holder standing in immediate relation with such signer is entitled to receive from him is proportionately reduced.

*Explanation.*—The drawer of a bill of exchange stands in immediate relation with the acceptor. The maker of a promissory note, bill of exchange or cheque stands in immediate relation with the payee and the indorser with his indorsee. Other signers may by agreement stand in immediate relation with a holder.

*Illustration*

A draws a bill on B for Rs. 500 payable to the order of A. B accepts the bill, but subsequently dishonours it by non-payment. A sues B on the bill. B proves that it was accepted for value as to Rs. 400, and as an accommodation to the plaintiff as to the residue. A can only recover Rs. 400.

**45.** Where a part of the consideration for which a person signed a promissory note, bill of exchange or cheque, though not consisting of money, is ascertainable in money without collateral enquiry, and there has been a failure of that part, the sum which a holder standing in immediate relation with such signer is entitled to receive from him is proportionally reduced.  
 Partial failure of consideration not consisting of money

**45.** A. Where a bill of exchange has been lost before it is over-due, the person who was the holder of it may apply to the drawer to give him another bill of the same tenor, giving security to the drawer, if required, to indemnify him against all persons whatever in case the bill alleged to have been lost shall be found again.

Holder's right to duplicate of lost bill  
 If the drawer on request as aforesaid refuses to give such duplicate bill, he may be compelled to do so.

## CHAPTER IV

### Of Negotiation

**46.** The making, acceptance or indorsement of a promissory note, bill of exchange or cheque is completed by delivery. delivery, actual or constructive.

As between parties standing in immediate relation delivery to be effectual must be made by the party making, accepting or indorsing the instrument, or by a person authorised by him in that behalf.

As between parties and any holder of the instrument other than a holder in due course, it may be shown that the instrument was delivered conditionally or for a special purpose only, and not for the purpose of transferring absolutely the property therein.

A promissory note, bill of exchange or cheque payable to bearer is negotiable by the delivery thereof.

A promissory note, bill of exchange or cheque payable to order is negotiable by the holder by indorsement and delivery thereof.

47. Subject to the provisions of section 58, a promissory note, Negotiation by bill of exchange or cheque payable to bearer is delivery. negotiable by delivery thereof.

*Exception.*—A promissory note, bill of exchange or cheque delivered on condition that it is not to take effect except in a certain event is not negotiable (except in the hands of a holder for value without notice of the condition) unless such event happens.

#### Illustrations

(a) A, the holder of a negotiable instrument payable to bearer, delivers it to B's agent to keep for B. The instrument has been negotiated.

(b) A, the holder of a negotiable instrument payable to bearer, which is in the hands of A's banker, who is at the time the banker of B, directs the banker to transfer the instrument to B's credit in the banker's account with B. The banker does so, and accordingly now possesses the instrument as B's agent. The instrument has been negotiated, and B has become the holder of it.

48. Subject to the provisions of section 58, a promissory note, Negotiation by bill of exchange or cheque payable to order, is indorsement. negotiable by the holder by indorsement and delivery thereof.

49. The holder of a negotiable instrument in blank may, without signing his own name, by writing above the indorser's signature a direction to pay to any other person as indorsee, convert the indorsement in blank into an indorsement in full; and the holder does not thereby incur the responsibility of an indorser.

50. The indorsement of a negotiable instrument followed by delivery transfers to the indorsee the property therein with the right of further negotiation; Effect of indorsement. but the indorsement may, by express words,

restrict or exclude such right, or may merely constitute the indorsee an agent to indorse the instrument, or to receive its contents for the indorser or for some other specified person.

### *Illustrations*

B signs the following indorsements on different negotiable instruments payable to bearer :—

- (a) "Pay the contents to C only."
- (b) "Pay C for my use."
- (c) "Pay C or order for the account of B."
- (d) "The within must be credited to C."

These indorsements exclude the right of further negotiation by C.

- (e) "Pay C."
- (f) "Pay C, value in account with the Oriental Bank."
- (g) "Pay the contents to C, being part of the consideration in a certain deed of assignment executed by C, to the indorser and others."

These indorsements do not exclude the right of further negotiation by C.

51. Every sole maker, drawer, payee or indorsee, or all of several joint makers, drawers, payees or indorsees, who may negotiate. of a negotiable instrument may, if the negotiability of such instrument has not been restricted or excluded as mentioned in section 50 indorse and negotiate the same.

*Explanation.*—Nothing in this section enables a maker or drawer to indorse or negotiate an instrument, unless he is in lawful possession or is holder thereof; or enables a payee or indorsee to indorse or negotiate an instrument, unless he is holder thereof.

### *Illustration*

A bill is drawn payable to A or order. A indorses it to B, the indorsement not containing the words, "or order" or any equivalent words. B may negotiate the instrument.

52. The indorser of a negotiable instrument may, by express words in the indorsement, exclude his own liability thereon, or make such liability or the right of the indorsee to receive the amount due thereon depend upon the happening of a specified event, although such event may never happen.

Where an indorser so excludes his liability and afterwards becomes the holder of the instrument, all intermediate indorsers are liable to him.

### *Illustrations*

(a) The indorser of a negotiable instrument signs his name adding the words—

"Without recourse."

Upon this indorsement he incurs no liability.

(b) A is the payee and holder of a negotiable instrument. Excluding personal liability by an indorsement "without recourse" he transfers the instrument to B, and B indorses it to C, who indorses it to A. A is not only reinstated in his former rights, but has the rights of an indorsee against B and C.

Holder deriving title from holder in due course.

53. A holder of a negotiable instrument who derives title from a holder in due course has the rights therein of that holder in due course

Instrument indorsed in blank.

54. Subject to the provisions hereinafter contained as to crossed cheques, a negotiable instrument indorsed in blank is payable to the bearer thereof even although originally payable to order.

Conversion of indorsement in blank into indorsement in full.

55. If a negotiable instrument after having been indorsed in blank is indorsed in full, the amount of it cannot be claimed from the indorser in full, except by the person to whom it has been indorsed in full, or by one who derives title through such person.

Indorsement for part of sum due.

56. No writing on a negotiable instrument is valid for the purpose of negotiation if such writing purports to transfer only a part of the amount appearing to be due on the instrument; but, where such amount has been partly paid a note to that effect may be indorsed on the instrument, which may then be negotiated for the balance.

Legal representative cannot by delivery only negotiate instrument indorsed by deceased.

57. The legal representative of a deceased person cannot negotiate by delivery only a promissory note, bill of exchange or cheque payable to order and indorsed by the deceased but not delivered.

**Instrument obtained by unlawful means or for unlawful consideration.**

58. When a negotiable instrument has been lost or has been obtained from any maker, acceptor or holder thereof by means of an offence or fraud, or for an unlawful consideration, no possessor or indorsee who claims through the person who found or so obtained the instrument is entitled to receive the amount due thereon from such maker, acceptor or holder, or from any party, prior to such holder, unless such possessor or indorsee is, or some person through whom he claims was, a holder thereof in due course.

**Instrument acquired after dishonour or when overdue.**

59. The holder of a negotiable instrument, who has acquired it after dishonour, whether by non-acceptance or non-payment, with notice thereof, or after maturity, has only, as against the other parties, the rights thereon of his transferor :

**Accommodation note or bill.**

Provided that any person who, in good faith and for consideration, becomes the holder, after maturity, of a promissory note or bill of exchange made, drawn or accepted without consideration, for the purpose of enabling some party thereto to raise money thereon, may recover the amount of the note or bill from any prior party.

### *Illustration*

The acceptor of a bill of exchange, when he accepted it, deposited with the drawer certain goods as a collateral security for the payment of the bill, with power to the drawer to sell the goods and apply the proceeds in discharge of the bill if it were not paid at maturity. The bill not having been paid at maturity, the drawer sold the goods and retained the proceeds but indorsed the bill to A. A's title is subject to the same objection as the drawer's title.

**Instrument negotiable till payment or satisfaction.**

60. A negotiable instrument may be negotiated (except by the maker, drawee or acceptor after maturity) until payment or satisfaction thereof by the maker, drawee or acceptor at or after maturity, but not after such payment or satisfaction.

## CHAPTER V

### Of Presentment

61. A bill of exchange payable after sight must, if no time or place is specified therein for presentment, be presented to the drawee thereof for acceptance, if he can, after presentment for reasonable search, be found, by a person entitled to demand acceptance, within a reasonable time after it is drawn, and in business hours on a business day. In default of such presentment, no party thereto is liable thereon to the person making such default.

If the drawee cannot, after reasonable search, be found, the bill is dishonoured.

If the bill is directed to the drawee at a particular place, it must be presented at that place; and, if at the due date for presentment he cannot, after reasonable search, be found there, the bill is dishonoured.

Where authorised by agreement or usage, a presentment through the post office by means of a registered letter is sufficient.

62. A promissory note, payable at a certain period after presentment of sight, must be presented to the maker thereof promissory note for sight (if he can, after reasonable search, be found) by a person entitled to demand payment, within a reasonable time after it is made and in business hours on a business day. In default of such presentment, no party thereto is liable thereon to the person making such default.

63. The holder must, if so required by the drawee of a bill of exchange presented to him for acceptance, Drawee's time for deliberation. allow the drawee forty-eight hours (exclusive of public holidays) to consider whether he will accept it.

64. Promissory notes, bills of exchange and cheques must be presented for payment to the maker, acceptor or drawee thereof respectively, by or on behalf of the holder as hereinafter provided. In default of such presentment, the other parties thereto are not liable thereon to such holder.

Where authorised by agreement or usage, a presentment through the post office by means of a registered letter is sufficient.

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**Exception.**—Where a promissory note is payable on demand and is not payable at a specified place, no presentment is necessary in order to charge the maker thereof.

**Hours for presentment.** 65. Presentment for payment must be made during the usual hours of business, and, if at a banker's, within banking hours.

**Presentment for payment of instrument payable at a specified period after date or time payable after sight thereof.** 66. A promissory note or bill of exchange payable at a specified period after date or time payable after sight thereof, must be presented for payment at date or sight.

**Presentment for payment of promissory note payable by instalment.** 67. A promissory note payable by instalments must be presented for payment on the third day after the date fixed for payment of each instalment; and non-payment on such presentment has the same effect as non-payment of a note at maturity.

**Presentment for payment of instrument payable at specified place and not elsewhere** 68. A promissory note, bill of exchange or cheque made, drawn or accepted payable at a specified place and not elsewhere must, in order to charge any party thereto, be presented for payment at that place.

**Instrument payable at specified place.** 69. A promissory note, or bill of exchange, made, drawn or accepted payable at a specified place must, in order to charge the maker or drawer thereof, be presented for payment at that place.

**Presentment where no exclusive place specified.** 70. A promissory note or bill of exchange not made payable as mentioned in sections 68 and 69, must be presented for payment at the place of business (if any), or at the usual residence, of the maker, drawee or acceptor thereof, as the case may be.

**Presentment when maker etc., has no known place of business or residence.** 71. If the maker, drawee or acceptor of a negotiable instrument has no known place of business or fixed residence, and no place is specified in the instrument for presentment for acceptance or payment, such presentment may be made to him in person wherever he can be found.

**Presentment of cheques to charge drawer.** 72. Subject to the provisions of section 84, a cheque must, in order to charge the drawer, be presented at bank upon which it is drawn before the relation between the drawer and his banker has been altered to the prejudice of the drawer.

## CHAPTER XIII

### Special Rules of Evidence.

118 Until the contrary is proved, the following presumptions Presumptions as shall be made —  
to negotiable instruments —

(a) that every negotiable instrument was made or drawn for consideration, and that every such instrument, of consideration, when it has been accepted, indorsed, negotiated or transferred, was accepted, indorsed, negotiated or transferred for consideration,

(b) that every negotiable instrument bearing a date was made or drawn on such date;

(c) that every accepted bill of exchange was accepted without time of in a reasonable time after its date and before its acceptance, maturity;

(d) that every transfer of a negotiable instrument was made as to time of before its maturity, transfer,

(e) that the endorsements appearing upon a negotiable instrument were made in the order in which they appear thereon,

(f) that a lost promissory note, bill of exchange or cheque as to stamp was duly stamped,

(g) that the holder of a negotiable instrument is a holder in due course. Provided that where the instrument has been obtained from its lawful owner, or from any person in lawful custody thereof, by means that holder is a holder in due course of an offence or fraud, or has been obtained from the maker or acceptor thereof by means of an offence or fraud, or for unlawful consideration, the burden of proving that the holder is a holder in due course lies upon him

119. In a suit upon an instrument which has been dishonoured, the Court shall, on proof of the protest, Presumption as presume the fact of dishonour, unless and until proof of protest such fact is disproved.

**120** No maker of a promissory note, and no drawer of a bill of exchange or cheque, and no acceptor of a bill of exchange for the honour of the drawer, shall, in a suit thereon by a holder in due course, be permitted to deny the validity of the instrument as originally made or drawn

**121** No maker of a promissory note and no acceptor of a bill of exchange payable to order shall, in a suit thereon by a holder in due course, be permitted to deny to payee's capacity, at the date of the note or bill, to indorse the same

**122** No indorser of a negotiable instrument shall, in a suit thereon by a subsequent holder, be permitted to deny the signature or capacity to contract of any prior party to the instrument

## CHAPTER XIV

### Of Crossed Cheques

**123** Where a cheque bears across its face an addition of the words "and company" or any abbreviation thereof, Cheque crossed between two parallel transverse lines, or of two generally parallel transverse lines simply, either with or without the words "not negotiable," that addition shall be deemed a crossing, and the cheque shall be deemed to be crossed generally

**124** Where a cheque bears across its face an addition of the name of a banker, either with or without the words "not negotiable," that addition shall be deemed a crossing, and the cheque shall be deemed to be crossed specially, and to be crossed to that banker

**125** Where a cheque is uncrossed, the holder may cross it generally or specially

Where a cheque is crossed generally, the holder may cross it specially

Where a cheque is crossed generally or specially, the holder may add the words "not negotiable"

Where a cheque is crossed specially, the banker to whom it is

**Crossed** may again cross it specially to another banker, his agent, for collection.

**126** Where a cheque is crossed generally, the banker on Payment of cheque whom it is drawn shall not pay it otherwise than crossed generally to a banker.

Where a cheque is crossed specially, the banker on whom it is drawn shall not pay it otherwise than to the Payment of cheque banker to whom it is crossed, or his agent for crossed specially collection.

**127** Where a cheque is crossed specially to more than one banker, except when crossed to an agent for the Payment of cheque purpose of collection, the banker on whom it is crossed specially more than once drawn shall refuse payment thereof.

**128** Where the banker on whom a crossed cheque is drawn has paid the same in due course the banker paying the cheque, and (in case such cheque has come to the hand of Payment in due course of crossed cheque the payee) the drawer thereof, shall respectively be entitled to the same rights, and be placed in the same position in all respects, as they would respectively be entitled to and placed in if the amount of the cheque had been paid to and received by the true owner thereof.

**129** Any banker paying a cheque crossed generally otherwise than to a banker or a cheque crossed specially Payment of crossed cheque out of due course otherwise than to the banker to whom the same is crossed, or his agent for collection, being a banker shall be liable to the true owner of the cheque for any loss he may sustain owing to the cheque having been so paid.

**130.** A person taking a cheque crossed generally or specially, bearing in either case the words "not negotiable," Cheque bearing "not negotiable" shall not have, and shall not be capable of giving a better title to the cheque than that which the person from whom he took it had.

**131** A banker who has in good faith and without negligence Non liability of received payment for a customer of a cheque banker receiving crossed generally or specially to himself shall not, payment of cheque in case the title to the cheque proves defective, incur any liability to the true owner of the cheque.

*Explanation.*—A banker receives payment of a crossed cheque for a customer within the meaning of this section notwithstanding that he credits his customer's account with the amount of the cheque before receiving payment thereof.

## CHAPTER XV

### Of Bills in Sets

132. Bills of exchange may be drawn in parts, each part being numbered and containing a provision that it shall continue payable only so long as the other remains unpaid.  
**Set of bills.** All the parts together make a set ; but the whole set constitutes only one bill, and is extinguished, when one of the parts, if a separate bill, would be extinguished.

*Exception.*—When a person accepts or indorses different parts of the bill in favour of different persons, he and the subsequent indorsers of each part are liable on such part as if it were a separate bill.

133. As between holders in due course of different parts of  
**Holder of first acquired part** the same set he who first acquired title to his part is entitled to the other parts and the money represented by the bill.  
**entitled to all.**

## CHAPTER XVI

### Of International Law

134. In the absence of a contract to the contrary, the liability of the maker or drawer of a foreign promissory note, bill of exchange or cheque is regulated in all essential matters by the law of the place where he made the instrument, and the respective liabilities of the acceptor and indorser by the law of the place where the instrument is made payable.  
**Law governing liability of maker, acceptor or indorser of foreign instrument.**

#### *Illustration*

A bill of exchange was drawn by A in California, where the rate of interest is 25 per cent. and accepted by B, payable in

Washington, where the rate of interest is 6 per cent. The bill is indorsed in British India, and is dishonoured. An action on the bill is brought against B in British India. He is liable to pay interest at the rate of 6 per cent. only : but, if A is charged as drawer, A is liable to pay interest at the rate of 25 per cent.

**135. Where a promissory note, bill of exchange or cheque is made payable in a different place from that in which it is made or indorsed, the law of the place where it is made payable determines what constitutes dishonour and what notice of dishonour is sufficient.**

**Law of place of payment governs dishonour.**

#### *Illustration*

A bill of exchange drawn and indorsed in British India, but accepted payable in France, is dishonoured. The indorsee causes it to be protested for such dishonour, and gives notice thereof in accordance with the law of France, though not in accordance with the rules herein contained in respect of bills which are not foreign. The notice is sufficient.

**136. If a negotiable instrument is made, drawn, accepted or indorsed out of British India, but in accordance with the law of British India, the circumstance that any agreement evidence by such instrument is invalid according to the law of the country wherein it was entered into does not invalidate any subsequent acceptance or indorsement made thereon in British India.**

**Instrument made, etc., out of British India, but in accordance with its law.**

**137. The law of any foreign country regarding promissory notes, bills of exchange and cheques shall be presumed to be the same as that of British India, unless and until the contrary is proved.**

**Presumption as to foreign law.**

## CHAPTER XVII

### Notaries Public

**138. The Local Government may, from time to time, by notification in the official Gazette, appoint any person, by name or by virtue of his office, to be a notary public under this Act and to exercise his power to appoint notaries public.**

functions as such within any local area ; and may, by like notification, remove from office any notary public appointed under this Act.

139 The Local Government may, from time to time, Powers to make notification in the official Gazette make rules for notaries consistent with this Act for the guidance of the public control of notaries public appointed under this Act, and may, by such rules (among other matters), fix the amounts payable to such notaries.

#### SCHEDULE

[ *Enactment repealed* ]

*Repealed by the Repealing and Amending Act, 1891  
(XII of 1891)*

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